OBSTACLES TO TRADE IN THE PACIFIC AREA

Proceedings of the Fourth Pacific Trade and Development Conference

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AUSTRALIA-JAPAN RESEARCH CENTRE

INTRODUCTION

The Fourth Pacific Trade and Development Conference was held in Ottawa, Canada, on October 7 to 10, 1971. The Conference program was outlined in the late summer of 1970, but it proved particularly topical in the wake of the currency and trade crisis following August 15, 1971.

Although the realignment of currencies agreed in December has eased international monetary relationships, trade problems remain. Especially in the Pacific area, the potential of trade as an engine of economic growth and as a basis for constructive political relationships is difficult to overemphasize. The mutuality of interests in international trade between the developed countries of the region is well known. Of increasing importance is the export potential and performance of developing countries in South and East Asia. The future record of industrially advanced countries in reduction or control of barriers to trade affecting developing countries' exports will test the sincerity of many who have professed to favour the liberalization of trade as a stimulus to development. The willingness and ability of developed countries to adjust their industrial structure will be the major theme of the Fifth Trade and Development Conference scheduled for Tokyo in January, 1973.

The Canadian host committee of the Fourth Conference in releasing the proceedings of the Conference wish to express appreciation to all those who have made possible the success of the Conference and the preparation of this volume. In particular, we wish to thank the public and private financial supporters in Australia, Canada, Japan, and the United States whose assistance has been essential. We also wish to thank those students, faculty, and staff members at Carleton who helped with local arrangements and the editing and preparation of the proceedings. The main responsibility for the latter task rested on Tom Burlington, who has recently gone to Japan to take up employment with the International Development Center of Japan.

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COMMUNIQUÉ

The Fourth Pacific Trade and Development Conference met at Carleton University, Ottawa, Canada, from October 7th to 10th to examine the considerable obstacles to trade and development that still exist among Pacific nations, and to suggest to policy makers how the trading relationships of this region can be improved. Previous conferences in this series have been held in Tokyo, Honolulu, and Sydney.

Participants from Japan, Australia, Singapore, Hong Kong, the United States and Canada, and from the International Bank for Reconstruction and Development and the Organization for Economic Cooperation and Development, engaged in an active discussion.

The conference was opened on October 7th with an address by the Hon. Jean-Luc Pépin, Minister of Industry, Trade and Commerce of the Government of Canada. Mr. Pépin asked participants to help governments to avoid the sacrifice of the long-term health of trading relationship in the pursuit of measures designed to deal with balance of payments problems.

Participants were well aware of the great timeliness of their meeting. They expressed deep concern about the implications of recent U.S. policy changes for the prospects of trade among countries of the Pacific rim.

Separate consideration was given to trade obstacles affecting the products of agriculture, the processed natural products (especially of the developing countries) and manufactures. In the discussion of trade in agricultural products it was emphasized that the agricultural policies of the United States, Europe and Japan impose important barriers to the exports from the countries of the Pacific region which can be efficient suppliers of grain and livestock products. The conference singled out U.S. policies to subsidize dairy products and thus meat products indirectly, and Japanese supports for rice and livestock production. It was pointed out that these practices distort allocation of resources in the agricultural sector, raise costs to other sectors of the economy, and significantly reduce the flow of trade in agricultural products.

The effect of trade and other policies upon the location of processing industries and the pattern of trade in processed products was also reviewed. The structure of tariffs which imposes much higher rates upon more processed forms of such products was criticized. These practices together with elaborate intergovernmental and intercorporate relationships make it difficult to estimate accurately the advantages which would be likely to accrue to developing countries if such institutional arrangements did not dominate trade. This applies particularly to sugar, petroleum, and some other products. In other cases, such as tropical wood products, it is more apparent that trade restrictions limit industrial expansion.

In the manufacturing sector, the countries of the Pacific rim face important trade obstacles. Three of the main developed countries of the region (Japan, Australia, and Canada) still retain higher tariffs on manufactures than most other developed countries. The conference discussed in some detail the major non-tariff barriers, in particular the scope and effects of voluntary export restraints, the long-term cotton textile agreements,

administrative barriers and government purchasing practices. The impact of the first two practices was covered in papers prepared by participants from Hong Kong and Singapore. The discussion brought out the serious implications for the future of exports of the developing countries of the restraints that penalise major sectors of manufacturing where successful development has occurred. Administrative and other non-tariff barriers, some outside the scope of GATT, were reviewed and found to have important effects on particular transactions. However, the conference found it difficult to assess their overall importance relative to remaining tariff barriers. Both in Japan and in the federal states, such as the United States, Canada, and Australia, the extent and effects of non-tariff barriers have proven difficult to determine. It was felt that further examination of specific non-tariff barriers was necessary and that new techniques would be required to keep such practices in check and to ensure that their impact would not seriously distort the country or product pattern of trade.

Participants were particularly concerned about the current policy environment including the lack of European interest in outward-looking trade policies, the growing protectionism in the U.S. reflected both in private groups and now in the actions of government, and the substantial levels of protection retained by other Pacific countries. Furthermore, the developed countries have shown only limited interest in providing access to their markets for the products of the developing countries.

The Conference Participants were troubled about the apparent inadequacy of the existing institutional framework; or at least the lack of positive initiative on the part of the governments operating within that framework. What appear particularly necessary are initiatives toward regional cooperation in the Pacific area in at least two directions.

(1) an effort on the part of developed nations to reduce and equalize trade barriers, so that Pacific nations among others can gain more of the advantages of specialization and exchange. In such circumstances, both they and the Europeans might be more willing to participate in new multilateral efforts toward trade liberalization.

(2) an effort to achieve more cooperation and integration among developing countries of the Pacific and a parallel effort by the developed countries of the region to provide better access for the products of the developing countries to their markets, so as to enlarge the flow of trade of these countries.

To this end the Conference favoured the establishment of a new intergovernmental institution including representatives from developed and less developed countries of the Pacific area, to study and promote practical means of achieving the foregoing objectives and to give particular attention to methods of monitoring barriers to trade and their effects. Further, such an agency should give particular attention to the study and promotion of effective and parallel adjustment assistance policies in the Paricif area countries.

The Conference applauded the purposes underlying the recent efforts of the United States Government and others to bring about realignment of currency values. Action is long overdue and is essential to achievement of more meaningful trade patterns. However, the Conference was deeply concerned about the method employed. In the first place it questioned the use of the surcharge as an element in the policy adopted, since these surcharges appear merely to postpone the realization of

meaningful currency relationships. Furthermore, the continuation of the surcharge for any substantial period seemed to the participants very likely to endanger the close trade relationships between the United States and its Pacific trading partners, and perhaps to have important political consequences as well.

Conference proceedings, consisting of papers submitted and a summary of points made in discussion, will be published shortly in order that the far-reaching issues debated may be available to all interested in the emerging patterns of trade and development in the Pacific region in the 1970s. The Steering Committee of the conference will later announce a venue and theme for the Fifth Pacific Trade and Development Conference.

Contents

Summary Policy Paper

SUMMARY: BARRIERS TO TRADE IN THE PACIFIC REGION*

THOMAS BURLINGTON

1. Introduction

Distortions and restrictions of international commodity trade continually impose serious losses of real income on Pacific area countries. Many of these distortions are unnecessary, and particularly biased against the less-developed countries of the region. These nations should be assisted rather than hindered by the policies of the developed countries. Most distortions arise from the policies of the Pacific nations themselves, but some are caused by the policies of outside countries, particularly those of Western Europe. While there are some possibilities of approaching the correction of these distortions on a global scale, most participants in the Fourth Pacific Trade and Development Conference felt that a promising approach — within the current world trading environment — is through regional initiatives and regional cooperation and negotiations.

This paper is a summary of the Conference participants' ideas and views on the most troublesome problems hindering freer trade and development in the area and suggestions for improving the situation. These problems have many facets and do not fit into a simple framework. The Conference was broadly concerned with the need for cooperation in trade liberalization and economic development of the Pacific Basin. The earlier working sessions were concerned with the following:

i trade in agricultural products — especially trade in grains and dairy and meat products;

ii factors influencing the location of processing industries in tropical countries, particularly factors related to trade barriers and industrial structures;

iii trade in manufactured products — the effects of voluntary export restraints on trade in textile products, the non-tariff barriers of Japan, and the government procurement policies of the United States were discussed.

Section 2 of this paper summarizes the attitudes in various countries of the region toward trade barriers, trade liberalization, and adjustment assistance programs for sectors subject to rapid and debilitating structural changes. A number of factors affecting the trade relations of the less-developed countries are also discussed. Section 3 of the paper discusses specific economic policies and obstructions to trade with regard to particular countries and commodities. This section grows out of the working sessions as described above. Section 4 briefly summarizes the main policy proposals brought forth at the Conference to enhance trade relations and economic development in the Pacific region.

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*This was separately published as an "Occasional Paper" by the School of International Affairs, Carleton University.

2. Attitudes and Factors Affecting Trade in the Pacific Area

The European Economic Community, the United States, and Japan are the most important trading entities in the world and have a major impact on trade relations among all countries in the Pacific region.

2.1. The Impact of the European Economic Community

The sheer size of the European Economic Community (EEC) bloc will increase considerably in the near future. Some of Britain's trade barriers will be increased, especially as a consequence of the Common Agricultural Policy (CAP). British entry will involve the end of Commonwealth Preferences, requiring adjustments in the Commonwealth countries. The wider application of the Common Agricultural Policy will lead to increasing self-sufficiency, especially in cereals and dairy products, and to increases in surpluses which will disrupt export markets around the world.

Arrangements will also be made with the European Free Trade Area (EFTA) countries for freer trade, especially in industrial products. Considering these arrangements and the special preferential arrangements the EEC has with the weaker Mediterranean and African countries, the voting bloc of the Community in international institutions will grow, perhaps to forty or fifty nations. Trade patterns in the Pacific region will be significantly affected by the policies of an enlarged EEC. In particular, the Community's propensity to disturb existing export patterns, its lack of interest in the problems of trading relations outside of Europe (two-thirds of European trade takes place within the bloc), and its determination to discriminate especially against the importation of the labour-intensive goods of East Asia are all major elements of the "policy environment."

2.2. Protectionist Trends and Adjustment Assistance in the United States

Many of the Conference participants felt quite pessimistic about the strong resurgence of protectionism in the United States recently. As Malmgren noted, this manifests itself in *ad hoc* trade restrictions, usually in the form of so-called "voluntary" import quotas, the inability to obtain authority from Congress for trade negotiations, and the near passage of generally restrictive trade legislation on more than one occasion since the end of the Kennedy-Round in 1967. The two major groups that had previously supported the move towards trade liberalization — the executive of the government and the labour unions — and which had helped hold the line against the very protectionist legislatures, have now begun to encourage the protectionist forces. While the executive has been searching for ways to adjust the U.S. economy to international trade, it also has political commitments, especially to the textile workers in the southern United States where government programs are in decline. The American labour movement has shifted from its traditional support of liberal trade policies to a new, quite intransigent, position favouring controls on both imports and direct investment outflows, particularly with regard to East Asia. This new emphasis has caused a major change, some participants called it a frightening change, in the direction of protectionism.

The Conference learned of the adverse attitudes of various American groups toward domestic adjustment assistance programs for depressed agricultural and relatively inefficient, often labour-intensive

industrial sectors. Such opposition is regrettable because carefully planned adjustment programs are usually the least-cost way of mitigating the effects of structural change and competition on less competitive industries. These programs can promote the reallocation of resources into more competitive and efficient channels.

Adjustment assistance programs in the United States are opposed on ideological grounds. Business is reluctant to support legislation for adjustment assistance because it is viewed as government interference with the free market. Paradoxically, tariffs and quotas are popular with businessmen. Government officialdom is reluctant because of the high budgetary cost of adjustment programs, although cost-benefit studies have not been carried out. The labour movement is opposed to the development of policies such as a comprehensive manpower program. It was emphasized that the adjustment assistance process will be an extremely difficult central issue of policy in the 1970s. Those industrial countries which handle it in the best way are the ones that will emerge from the process least strained.

Neo-mercantilist tendencies have been building up for a number of years, and have recently been aimed especially at goods from East Asia. Beginning with agitation for textile import quotas in the early 1960s, the pressure has spread to other labour-intensive products and has intensified. Frustrations with EEC policies, growing competition from Japan, the weak state of the domestic economy, and the chronic balance of payments deficits have added to the political frustrations over the Vietnam War and the unequal distribution of the economic burden of defence among Western countries. This turning inwards has left in abeyance a number of initiatives of the United States on various aspects of foreign aid and development expenditures and the implementation of general tariff preferences.

The American participants agreed that it is necessary for measures and action to be taken immediately to counteract this neo-mercantilist trend but they were pessimistic that such action would be generated inside the United States. The Guam Doctrine embodying a substantial shift in the American role in Asia leaves an important external pressure point open in the form of "supporting the initiatives of other nations." This has been interpreted more in terms of initiatives in a security sense. Some participants suggested, however, that serious economic initiatives fostering methods or institutions for greater regional cooperation, especially if taken by Japan, would be very helpful in trying to shift the United States out of its present mode of behaviour.

2.3. Japan

2.3.1 Japanese Attitudes toward Trade Barriers

Conference delegates felt that attitudes of important Japanese organizations toward liberalization of trade and development relations in the Pacific were more difficult to characterize than the attitudes of the EEC or the United States. The level of trade barriers still remains unquestionably high in Japan. Non-tariff barriers such as state-trading, residual import restrictions or quotas contravening GATT agreements are very important in agriculture. In the manufacturing sector, barriers are also high, but the relative importance of tariff and non-tariff barriers is more difficult to determine, principally because of a lack of data. On the other hand, the trend towards removing trade barriers which contravene the GATT agreements has been

rapid in recent years, due to the growing balance of payments surpluses since 1968, the continuing advance of Japanese consumer prices, and external political pressures especially from the United States.

A leading Japanese participant argued that the most important factor speeding Japanese trade liberalization was anxiety over the growing protectionist tendencies in the United States. Before the Japanese-American textile negotiations and the plethora of anti-dumping cases during 1969 and 1970 against imports from Japan, both the Japanese government and the general public did not really recognize that the very existence of the Japanese economy depends upon relatively free, multinational trade. Up until then, Japanese government officials and leading businessmen paid lip service to free international trade, but there simultaneously prevailed a belief that free trade mainly benefitted the most advanced, most "powerful" countries, e.g., England in the nineteenth century or the United States today. It was hardly surprising that Japan got into a frame of mind of strictly regulating imports. Furthermore, Japan first entered export markets in the 1920s and 1930s, and soon faced very high import barriers imposed by the developed nations and their colonies, which were designed to divert the main thrust of Japanese trade. This situation was not an insignificant factor in provoking Japanese entry into the Second World War.

However, now that the United States has begun to turn toward protectionism, many Japanese for the first time realize that Japan does benefit a great deal from free world trade. Given this realization, Japanese leaders are faced with the problem that it is not only difficult to dismantle trade barriers, it is also difficult to dismantle a protectionist frame of mind which has become counter-productive for Japan.

An American participant noted that a major element in the 1970-71 American policies on trade was a collision with Japan, both officially and on the level of private business activities in the Pacific. A mood of hostility and protectionism in the United States has grown rapidly among certain important segments of the American political and economic system. In a similar vein, concern was expressed about the degree of conflict between reality and image concerning Japanese administrative guidance. Japan has acquired an image in the United States of "Japan, Inc." This idea grows from the notion that government-business cooperation is so universal that a special set of rules are necessary for dealing with Japan. Quantitatively, there seem to be many individual stories about these difficulties with Japan, and while they may be relatively few or of small importance, the issue has been greatly magnified. Conference delegates argued that hard data is needed to evaluate these stories, to confirm or dispel this image. A variety of other factors related to both Japan and other East and South East Asia countries was mentioned as giving rise to this mood of hostility:

i The export successes of Japan, Korea, Taiwan, and Hong Kong have generated strong policital reactions in importing countries.

ii Some American companies have built processing or assembly facilities in this area, to bring in products formerly produced in the United States. The major examples are in the electrical and electronics industry.

iii American manufacturers discovered that European countries have maintained a number of formal and informal controls on imports from Eastern Asia on what is essentially a discriminating basis. This is interpreted as a major cause of the concentration on the United States and Canadian markets for the exports of manufactures from Eastern Asia.

2.3.2. Adjustment Assistance in Japan

An important element in the trade and development policies of the developed countries is their attitude toward adjustment assistance programs to smooth out the process of structural change. This is particularly important to Japan with its very high rates of growth and structural change. It was noted that Japan has an effective industrial policy that shifts resources out of inefficient sectors and pushes them into industries that have high future productivity. By contrast, the United States claims that it does not have an industrial policy, and that structural change is simply the sum of market forces. In reality, the United States does have such a policy, but it is made up of a number of *ad hoc* measures which end up protecting inefficient industry. The United States does not favour Japan's approach, claiming there is too much government interference with and direction of industry.

A Japanese participant carefully explained the structural difficulties besetting the Japanese agricultural sector and sketched why it was necessary to have an explicit policy to deal with them. He argued that Japan should abolish agricultural protection to the benefit not only of exporting countries, but also, in the long run, of Japan. There is a real problem of rural poverty in Japan. The poorest farmers, who number one-quarter of the farm population, cannot be moved for reasons of age and opportunity. This is a particularly awkward problem since the Ministry of Agriculture apparently does not have an articulate, consistent adjustment policy and in fact general agricultural policy in Japan is virtually moribund.

A number of proposals were made at the Conference to improve trade and development relationships in the Pacific. These will be discussed later, but it is important to note here that all participants hoped that Japan would play a cooperative role and take significant initiatives in these respects. The Japanese are pessimistic about the possibilities for global liberalization; only an enlarged EEC is visible on the horizon. The Japanese government will take neither a "going ahead" nor a "falling behind others" stance in trade policy. But in that kind of "trade policy in disguise," the Japanese government may actually pursue a measure of regional integration with Australia and the South East Asian countries. Canada would be welcome to join in. Also, the Japanese government will favour a set of policies for the internal restructuring of the economy so that the economy would not be in a disadvantageous position if there were a swing toward global free trade around 1980. Japan wishes to go along with the United States ultimately, but at present the United States is too big and too tough, so that moves toward a modest Pacific integration appear to be a good strategy.

2.4. The Less-Developed Countries

2.4.1. The Bias of Trade Barriers

It is well known that the trade policies of the developed countries are biased against the less-developed countries and particularly against the countries of East and South East Asia. Balassa's calculations, given in Vandendriessche's paper,[1] of pre- and post-Kennedy-Round effective tariff rates show that not only are rates biased against the LDCs, but also tariff reductions brought about by the Kennedy-Round were proportionately lower

[1] "Factors that Influence the Location of Processing Industries in Tropical Countries," Henri Vandendriessche.

on products of interest to LDCs than on more advanced manufactures. Non-tariff barriers such as quotas, "voluntary" restraints, and price-subsidy policies are also very important. On the other hand, the recent U.S. surcharge was thought not to affect the exports of the less-developed countries very much. Most of their exports to the United States are either regulated by quotas or incorporate a small amount of value added in the country by American-owned subsidiaries. The surcharge does not apply to goods regulated by quotas and has only a small effect on the latter category of exports.

2.4.2 The Competitiveness of the Less-Developed Countries

It was mentioned above that the competitiveness and energy of most East Asian countries have stimulated U.S. protectionist moves especially towards more labour-intensive products, as well as giving rise to particularly discriminatory barriers in Europe. One participant observed that it is not Japan that the United States need be worried about in future; rather it is the six or seven "Japans" coming up. As well as the traditional labour-intensive products like toys and textiles, imports into the United States from LDCs now include steel, hydroelectric generators, and complicated electronics circuitry. It is commodities of this sort that will dismay developed countries by their range and sophistication. Products from countries like Argentina, Columbia, and Brazil as well as the East Asian countries are able to penetrate developed markets despite tariff barriers. For example, Hong Kong and Singapore have a comparative advantage over the developed countries in a number of important products. In these industries they have a technology which is similar to or more advanced than that in the developed countries, good management, experienced labour and commercial services, and low wage levels. Consequently, in items in which value-added is significant, they can jumb over any tariff barriers that the developed countries can reasonably put up. This is an important reason why the developed countries have moved from tariff barriers to quantitative restrictions. The cut-off point when quantitative restrictions are thrown up seems to occur when penetration reaches 5 percent of the developed country's market for a general range of products and 20 percent for specific products. When potentially big economies such as India and Brazil get moving, these saturation levels will be approached very swiftly, resulting in strong measures to limit imports at that level by a proliferation of voluntary restraint agreements.

2.4.3. The Need for Adjustment Assistance in Developed Countries

Thus, if the developing countries as a whole are going to be able to trade with the developed nations on an effective scale, there must be a new stress on adjustment assistance in the developed countries to allow such changes to take place. The marginal productivity of workers in Hong Kong and Singapore is higher today than the marginal productivity of workers in parts of the United States, Australia, Canada, and many European countries. It is easier to retain the Singapore and Hong Kong workers who are on the whole better educated than, for example, the workers who will be displaced in the garment industry in the southern United States. Therefore, adjustment assistance needs to be a broader policy than the training of a few thousand workers here or there, so that in fifteen years time when this question becomes acute there will be a new basis for world trade rather than the economic confrontation that could lead to very serious political consequences.

2.4.4 Protectionism in Less-Developed Countries

Another aspect of the trade barrier problem that the LDCs face is due to what was called the postwar reaction to the prewar division of labour, which led to import substitution policies and very high tariffs among the LDCs themselves. Many inefficient production units have been established behind these trade barriers, making it difficult for each country to specialize and trade with its neighbours.

The problem is further accentuated in those countries that have large labour forces employed in weak, protected sectors. In rich countries with good social security at a period of rapid growth, the problems are not too great. However, in countries with huge employment problems, low standards of living, high rates of population growth, and low rates of economic growth, the problems are enormous. Tariff barriers must be dismantled, but it is much more difficult for many LDCs than for advanced countries.

2.4.5. The Effects of Generalized Tariff Preference Schemes

The EEC, Japan, and Australia have implemented generalized tariff preference schemes, and the U.S. scheme has been proposed. Malmgren[2] was very pessimistic about the effects of these schemes on liberalizing trade with the developing countries. He noted that the U.S. scheme has not even been sent up to Congress in the form of proposed legislation because the Executive rightly fears transformation of any trade legislation into protectionist legislation of a different character altogether. If implemented, the U.S. scheme would have safeguards against market disruption in the form of exceptions made for "sensitive" labour-intensive products and an escape clause procedure. The latter escape procedure would probably be sought by U.S. manufacturers and workers fairly frequently; and the Tariff Commission, if it followed its other recent practices, would probably often support snap-backs to the MFN rate. The uncertainty generated would be high.

The Community general preference scheme offers certain theoretical advantages over the American scheme, looking at the whole of the developing world together. The Community would first of all not invoke a safeguard (snap-back to MFN rates) unless imports from preferred countries had reached a certain trigger level. The trigger would be observable, in theory, and therefore countries could plan more effectively. Second, the Community would place imports of a certain product from a given country back into the MFN category if that country's exports of the item exceeded one-half of the total volume allowed under the ceiling or trigger level. This would mean that countries which became relatively strong competitors would be moved into normal competition with the developed countries, making room for the lesser developed countries to use preferences to develop a capability to export. The Community began to implement the scheme in the summer of 1971, but it is not all that it seems. Based upon analysis of the specific mechanics, R. N. Cooper has concluded that the Community scheme as now implemented will offer almost no additional incentive to developing countries to export. The tariff quotas have been set on a base of 1968, with a low add-on allowance. The rate of growth of successful exporters is such that they will end up exceeding the tariff quotas in the initial period. Moreover, Vendendreissche pointed out that the preferences mostly apply to all the manufactured goods but not to the agricultural processed goods which are important to Asian

[2] "Trade Liberalization and the Economic Development of the Pacific Basin: The Need for Cooperation," Harald B. Malmgren.

countries. There were also some major exceptions in the manufactured goods category, such as textiles and labour-intensive processed goods like handicrafts, so that for commodities which the preferences might have assisted, they were not instituted.

Under the Japanese scheme, preferences affect only 4 percent of imports to some unspecified extent. In Australia, the preferences are purely nominal, affecting much less than 1 percent of imports with a margin of perhaps 1 to 2 percentage points on tariff levels around 40 percent.

The actual mechanics of these schemes will effectively block access to developed markets for a majority of East Asian products. As a result, the LDCs could be expected to be somewhat bitter about this type of program. Many of them have already discounted preference schemes as a means to export expansion.

2.4.6. Unemployment and the Green Revolution

There are a number of important influences on current and forthcoming Asian trade patterns, such as the unemployment situation, the effects of the green revolution, and the withdrawal of the United States from Vietnam and the end of the war. It was argued that the rapidly growing unemployment problem in LDC Asian economies is reaching a critical stage. This phenomenon is not stressed nearly enough and will overshadow many of the trade topics discussed by the Conference. Unemployment has been widely ignored either because data are lacking or because quantified information on employment is misleading. As a first step, great efforts are needed to generate more and better data. With this at hand, questions of the impact of unemployment on trade policy and the ways in which trade policy can ease the situation could be carefully considered.

Malmgren suggested that the hybrid seeds of the Green Revolution and technological progress generally have enabled South Asia and parts of South East and East Asia to become nutritionally self-sufficient and have somewhat deceptively allowed hopes of export potential to rise. Furthermore Japan as a developed nation is self-sufficient in rice with large surpluses that can be dumped as food aid. Japan has very high agricultural support prices, as do many of the developing countries themselves, and in both cases such policies have contributed to recent expansions in production. Thus, because of the tendency toward widespread self-sufficiency and for other reasons, the future of export markets in food grains looks bleak, and hopes for the evolution of South East Asia as the "rice bowl" for the rest of Asia are probably misguided. This applied also to South Vietnam in the postwar period. The Green Revolution will also likely exacerbate the unemployment problems in these countries, thus slowing down the adoption of new agricultural techniques. The real potential of this area in agricultural trade, so far as there is one, is higher up the protein ladder, first in feed supplies and eventually, as incomes grow, in the production of meat.

2.5. Canada and Australia: Protectionist Attitudes and Structural Problems

Finally, the situation in the other developed countries of the Pacific region is of interest. While Canada and New Zealand were not mentioned much during the Conference, it seems that in Canada at least protectionist sentiments are not on the wane and if anything are increasing,

partly in reaction to Canada's relationships to the United States. Canada, Australia, and Japan are among the countries with the highest trade barriers in the world, especially in processing and manufacturing. A number of commentators pointed out that Australia is among the countries with the most experience in raising protective trade barriers. Now that even wool is subsidized, there is almost nothing that Australia hasn't tried to protect. However, the paper written by the Australians, Crawford and Board,[3] stood out at the Conference as one which made some concrete, negotiable proposals, especially with respect to trade negotiations with Japan and possibly including other Pacific countries. They were particularly interested in the reduction of barriers to Australia's agricultural exports in return for the formulation of a mineral resources policy and reductions in very high tariff rates. There was a note of caution when they stated that the political climate in Australia at present is much more favourable for alterations in tariff rates than in the past. However, the balance of forces in Australia is such that considerable gains would have to be in sight before any significant action outside the long process of Tariff Board review could be contemplated.

Of course Canada and Australia, like all developed countries, have important structural problems to face in the agricultural sector. Drysdale summarized the main message of the Crawford-Board paper: agriculture plays a vital role in the Australian economy and trade, so that the decline in farm incomes due to falling export prices for agricultural products and substitution of synthetics for wool has caused great structural difficulties to which adjustments must be made. But the extent, pace, and cost of these adjustments will depend importantly on Australia's assessment of the world farm trade outlook and her ability through negotiation to gain increased access to trade outlets. However, commenting on the paper, Drysdale also noted the far more difficult situation in the developing countries and also that, in a quiet way, Australia has become a very big surplus country along with Japan and West Germany during 1970-71. Therefore, it seems quite within Australia's means to help her own farmers by reducing tariffs across the board or by other means.

Canadian commentators noted that Canada has similar structural problems to Australia and mentioned some of the thorny political problems impeding adjustment. Dealing with adjustment assistance and non-tariff barriers in countries with a federal structure is particularly cumbersome. Adjustment assistance in Canada is usually a question of regional development involving heavy capital and labour subsidies, but these subsidies may be just a new form of protection. While they are one-time subsidies, they are so large that they may produce continuing problems, particularly since the beneficiary firms are often members of industries into which the developing countries will want to move in the next decade. Concern was expressed that what is intended to be an adjustment assistance program can be transformed by businessmen into a new protective program within a few years. Related to this, it was suggested that many non-tariff barriers (NTBs) come under provincial or state powers and have a direct regional impact. Many such items subject to NTBs are connected with political patronage for particular groups. Because regional development, subsidies, state and provincial procurement involve deals that are much more amenable to political patronage than tariffs, they are consequently more difficult to eliminate than tariffs.

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[3] "Japan's Trade Policy and Trade in Temperate Zone Agricultural Products," J. G. Crawford and G. H. Board: Professor Peter Drysdale of Australian National University opened the discussion on this paper.

2.6. Policies to Facilitate Trade Negotiations and Economic Cooperation in the Pacific Region

A wide variety of policies have been suggested in recent years at these conferences and in many other forums for promoting greater world trade liberalization and regional cooperation in both trade and other matters in the Pacific area. Richardson and Baldwin[4] pointed out that the present state of exchange-rate flexibility and the contemplated future state of exchange-rate realignment provide an ideal opportunity, if not an invitation, for all countries to eliminate non-tariff barriers. Their views are explained in the final section of this paper.

By adoption of broadly-conceived adjustment assistance programs by the developed countries is essential in soothing the severe strains and stresses that may be inflicted by rapid structural changes in the economic systems of these countries. It is essential for the developed countries to reduce trade barriers on either a general or a preferential basis, both to ease hindrances to the development of the less-developed countries and to achieve a better allocation of world resources. The less-developed countries must also reduce trade barriers among themselves. The developing countries must adopt better methods of conferring and coordinating their policies and actions vis-à-vis the developed countries, for much of the discrimination practised by the developed against the less-developed countries has been achieved partly because of a lack of collaboration among the less-developed countries.

While most of the participants were quite pessimistic about the potential for global trade liberalization negotiations at least in the intermediate term, there was much emphasis on the need for developing a regional framework within which inter-governmental discussions and negotiations could take place. A Pacific Area Free Trade Agreement, such as suggested by Professor Kojima in recent years, appears to be somewhat premature considering the many problems in its path. However, in view of the current atmosphere surrounding trade relations and the current attempts to establish revised international monetary mechanisms, the participants at the Conference agreed that the next year was propitious for the establishment of a regional institution along the lines of OECD to provide the government-to-government consultations. Crawford and Board mentioned that, although this is already a function of OECD, Japan, Australia, the United States, and Canada are the only non-European nations out of a total OECD membership of twenty-three. Thus there would appear to be considerable advantage in having a smaller-scale regional organization to deal with problems of a more regional nature that may well be frustrated in OECD, or even in GATT, in which European interests tend to impede world-wide progress.

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[4] "Government Purchasing Policies, Other NTBs, and the International Monetary Crisis," R. E. Baldwin and J. D. Richardson.

[5] K. Kojima, "Japan's Interest in the Pacific Trade Expansion, *"Papers and Proceedings of the First Conference on Pacific Trade and Development,* Tokyo, Japan Economic Research Center, 1968.

Agricultural Trade

JAPAN'S TRADE POLICY AND TRADE IN TEMPERATE ZONE AGRICULTURAL PRODUCTS[1]

by

J. G. CRAWFORD and G. H. BOARD

This paper examines Japan's agricultural trade policy from the point of view of Australia, a large and efficient agricultural exporter, and one whose comparative advantage has been frustrated by protectionist agricultural trade policies throughout the world. First, the critical state of agriculture in Australia is discussed to highlight Australia's concern about agricultural protectionism and her desire to gain increased access to overseas markets. Next the importance of Japan as an importer of farm products is stressed and the background to, and current position of her restrictive commercial policies toward agricultural trade are examined. The interests of the other three major farm product exporters in the Pacific area, the United States, Canada and New Zealand, in the Japanese market are then examined. It emerges that Japan's agricultural trade has a big role to play in forcing the pace against protectionism generally, and especially in the Pacific region.

1. Australian Agriculture and Trade

1.1 The Critical State of Australian Agriculture

At the beginning of the seventies Australian agriculture is in a critical state. Aggregate farm income in 1970-71, at $A891 million, was the second lowest since 1949-50 and well below the $A1,431 million earned in 1963-64.[2]

Despite a fall in the number of farm operators, especially over the past few years, average income per farm operator (owner, lessee or share-farmer) in 1970-71 had declined to about $A4,500 and in real terms was 45 per cent below the 1963-64 level. Projections of aggregate farm income in 1974-75 show a further fall to $A860 million.[3] By contrast, non-farm real incomes have risen steadily, and are expected to continue this trend.[4]

The figure, average income per operator, conceals considerable variation, both between farms and different rural industries. Data from surveys of some rural industries carried out by the Commonwealth Bureau of Agricultural Economics, show that, in the mid-sixties, apart from the wheat industry, at least 20 per cent of producers in the sheep, beef, dairy and fruit industries had net farm incomes less than $A2,000.[5] In a number of these

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[1] The authors would like to thank Mrs. P. Brown for her considerable efforts in the preparation of this paper.

[2] Aggregate farm income is equal to the gross value of rural production minus total farm costs. Appendix 1 contains definitions of these terms together with data from 1960-61 to 1970-71.

[3] 'A Projection of the Rural Sector, 1974-75', contained in Bureau of Agricultural Economics, *Debt Reconstruction and Farm Adjustment*, Canberra, February 1971.

[4] Between 1963-64 and 1970-71 average weekly earnings per employed male in Australia increased by 26 per cent in real terms. See Commonwealth Bureau of Census and Statistics, *Monthly Review of Business Statistics*, June 1971.

[5] Net farm income is defined as gross returns less cash costs and allowances for unpaid family labour (not including the operator) and depreciation. The residual provides the return to the owner-operator for his labour and management and also for the capital employed, including funds needed for the servicing of debt.

industries the percentage was much higher, for example, in the dairy industry it was 56 per cent.[6] For the rural sector as a whole it was estimated that in the early part of the sixties about 80,000, or around one third of the total number of farms in Australia were earning net farm incomes less than $A2,000.[7] This yardstick is by no means high; it compares with the legal minimum adult male wage in Australia in 1967 of $A1,990, and average employed male earnings in that year of $A3,160, and indicates that large numbers of farmers were living on depreciation and thus eroding their capital base. Since that estimate was made, average greasy wool auction prices have fallen by over 60 per cent and prices for most other farm products have remained static or declined.

Perhaps the only bright spot in the Australian rural sector at the present time is the buoyant price of beef. In striking contrast to most other rural products beef prices in 1970-71 were about 38 per cent above the levels ruling ten years earlier. Many farmers in livestock-grain areas, adversely affected by the price falls in wheat and wool and the quota restrictions on wheat have already begun to diversify into alternative crops such as feedgrains and oilseeds, and the grazing of beef cattle. Unfortunately many farmers are in areas where alternative enterprises to wool are not feasible, and many more in all industries are in such a poor financial position and so heavily in debt that they are unable to carry on, let alone borrow to invest in land use changes.[8]

This dramatic decline in farm incomes can be attributed to a number of factors. Farm incomes in Australia have been under considerable pressure from rising costs on the one hand and static or declining returns on the other. This 'cost/price' squeeze has intensified over recent years. (See index of the ratio of prices received to prices paid in Appendix 2).

Over the last decade aggregate farm costs have risen at about 5 per cent per year. About half of this increase was due to greater input usage, brought about in large measure by efforts of farmers to increase productivity. The remainder is attributable to increases in the price of inputs. The cost increases have been brought about mainly by the inflationary pressures of growth in a full-employment economy and in part by the effects of generous tariff protection of domestic industry. Australia's protection of domestic manufacturing industry has a direct effect on farm costs, and further, it contributes to inflation by enabling industries sheltering under the tariff wall to pass on cost increases such as higher wages. Although the rise in unit costs over the last decade has been, on average, a little over 2 per cent per annum, which is not high by international standards, the fall in prices over recent years, especially for wool, has been such that farmers have been unable to offset the dual effect of rising costs and falling prices by their traditional means of increasing productivity.

While farmers are able to influence domestic prices of certain products such as sugar, wheat and butter, to some extent, the domestic market is growing so slowly and such a large proportion of Australian rural output is exported, that prices on overseas markets have a heavy influence on overall

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[6] See *Debt Reconstruction and Farm Adjustment, op. cit.*, p. 182.
[7] D. H. McKay, 'The Small Farm Problem in Australia', *Australian Journal of Agricultural Economics*, Vol. 11, No. 2, December, 1967.
[8] Total rural debt outstanding to major institutional lenders has more than doubled over the past decade, and at $A2,095 million in 1970, was over twice the level of aggregate farm income. See 'The Australian Farm Situation 1970-71', *Quarterly Review of Agricultural Economics*, Vol. XXIV, No. 1, January 1971.

farm returns. (See Appendix 2) Normally over half of Australia's total rural output is exported but the relative importance of domestic and export markets varies between commodities. For example, over 95 per cent of wool produced is exported, and for some other products the proportions are, wheat 74 per cent, sugar 70 per cent, beef 46 per cent and butter 42 per cent.[9]

A number of influences have been at work which have contributed to the erosion of farm prices. The advance of technology, and in particular the development of substitutes for rural products, has had a severe effect on Australia through the inroads made into the wool market by synthetic fibres. In addition, technological and managerial advances have had a considerable impact on the levels of agricultural productivity and production throughout the world. Further, in most developed countries incomes and consumption of agricultural products are already at relatively high levels and overall market growth is slow. But from the point of view of efficient agricultural exporters, the most blatant and to them unnecessary hindrance to market growth is the highly protectionist commercial policies that are pursued by advanced industrial countries.

1.2 Protectionism in the EEC, UK and Japan

The Common Agricultural Policy (CAP) of the European Economic Community is the most comprehensive and effective of all systems of agricultural protection, and from the point of view of exporters in the United States, Canada, New Zealand and Australia the situation will be greatly aggravated by the entry of Britain into the EEC.

The CAP includes a common external tariff on most agricultural products, a system of variable levies on many products to insure against competition over the tariff barriers, and also quantitative restrictions.[10] In addition, the export of surplus production generated by the lavish price incentives, is encouraged by export subsidies, known as 'restitution payments', which are sometimes greater than the ruling world prices.[11] The CAP covers about 90 per cent of EEC agricultural production and included under its protectionist umbrella are wheat, coarse grains, rice, sugar, diary products, beef, eggs, and fresh fruit which are all important Australian exports, especially important now because of the collapse of wool prices. Some idea of the absurdly high levels of protection granted under the CAP can be gained from Appendix 3 which shows the overall value of the variable levies charged as a percentage of the average c.i.f. import price in 1968-69 for a number of important commodities. These figures indicate that for cereals the sizes of the variable levies range up to 98 per cent of the average c.i.f. import prices, while for sugar and butter the percentages are 230 and 403 respectively. It is clear that the CAP is designed to allow imports only to the extent that EEC production fails to reach the quantity demanded at the prices fixed to maintain agricultural incomes.

The value of Australian farm exports to the EEC in 1969-70, $A336 millions, was the same as in 1963-64, but the total value of farm exports excluding wool and skins, which account for over 80 per cent of

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[9] *ibid.*

[10] See Brian Fernon, *Issues In World Farm Trade: Chaos or Cooperation*, Atlantic Trade Study, Trade Policy Research Centre, London 1970, pp. 43-44.

[11] Harald B. Malmgren, *Trade Wars or Trade Negotiations: Nontariff Barriers and Economic Peacekeeping*, The Atlantic Council of the United States, 1970, p. 42.

these exports, declined by almost 24 per cent over the same period. The importance of the EEC market for Australian farm exports has diminished year by year, and from taking one quarter of farm exports in the mid-fifties its share was down to about 11 per cent or $A245 million in 1970-71, $A91 million below the 1969-70 level. (See Appendix 4). This fall in the value of Australian agricultural exports to the EEC over the last year was due entirely to the sharp decline in wool prices.

An even more striking decline in importance as an overall market for Australia's agricultural output has occurred with the United Kingdom, which for so long was Australia's premier market. During most of the fifties about one third of Australia's rural exports was shipped to the United Kingdom but over recent years its share has only been 14-15 per cent. The fall of over $A100 million in farm sales to the United Kingdom is almost wholly due to a drop of 50 per cent in quantity of wool exported and a fall of over 40 per cent in its price. But in post-war years the United Kingdom has also adopted agricultural policies aimed at greater self-sufficiency in farm produce. In recent years it has amended its methods of protection, moving them closer to the methods adopted in Europe. Higher output of beef and cereals is being encouraged and since the early sixties measures such as import quotas, voluntary import restraints, and minimum import price schemes have been introduced for all major temperate zone foodstuffs except mutton and lamb, and these now attract a duty.[12] As a result of rising domestic production, slow growth in total demand, and import curbs, Britain's food imports have been virtually static over the past decade. The strong likelihood of Britain's entry into the EEC and its adoption of the CAP will mean increased domestic production and a greater part of Britain's imports of some products such as soft wheat, sugar, and butter will be supplied by the enlarged EEC and its associate members.[13] The diversion of continental surpluses to the United Kingdom, particularly dairy products, and wheat, will temporarily ease the pressure of EEC exports in other world markets. However the potential for increased production in an enlarged EEC under the generous incentives of the CAP is so great that this respite is likely to be temporary.

In the face of the highly protectionist policies in Europe, the stagnation of the British market and the impending entry of the United Kingdom into the protectionist camp, there has been a remarkable transformation in the direction of Australia's agricultural trade, especially over the last decade. (See Appendix 4).

Japan and North America, particularly the United States which imports large quantities of Australian beef and sugar, have taken the places of Europe and the United Kingdom as major export markets. Japan has emerged in recent years as Australia's major export market, accounting for over 20 per cent of agricultural exports and 27 per cent of total exports, and is a principal market for wool, mutton, cheese, wheat and sugar. (See Appendix 5). However, a highly protected domestic agriculture is not the preserve of Europe. Australian (and other countries') exports of beef, mutton, most dairy products, and sugar to the United States are limited by quotas, while wool attracts a tariff of 25 cents per pound (compared with

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[12] G. M. Sanders, 'Recent Trends in United Kingdom Agricultural Policy', *Quarterly Review of Agricultural Economics*, Vol. XXIII, No. 2, April 1970.

[13] Denmark, Norway, and Ireland have also applied to join the EEC.

current average auction prices of 29 cents). Similarly, Japan maintains strict controls over the import of a number of major temperate zone agricultural products.

Despite this re-orientation of Australian agricultural trade, a number of important Australian rural exports are still heavily dependent on the dwindling United Kingdom market. Not only does the United Kingdom account for a significant proportion of Australian exports of butter, cheese, wheat, sugar, fruits, mutton and lamb, these exports to the United Kingdom are, in a number of cases, a significant proportion of total Australian production. (See Appendix 6). The seriousness of the situation is heightened by the fact that the production of dairy products, sugar and fruits is concentrated in a number of areas where the incomes of large numbers of people are directly dependent on the continuing health of these industries.[14] Even though Japan has taken increasing quantities of Australian wheat, sugar, cheese, beef and mutton, exports of these products together with butter, fruits and a number of other commodities all run up against significant trade barriers in that market.

1.3 The Outlook for Australian Rural Exports

The bleak outlook for rural exports would not be so serious were it not for the fact that rural exports play such a vital role in the Australian economy. In terms of the proportion of the total workforce employed, (8.1 per cent in 1969-70)[15] and its contribution to the Gross National Product, (5.8 per cent in 1970-71, down from 10.4 per cent in 1966-67)[16] agriculture plays only a minor role in the economy. However, the agricultural sector still accounts for 50 per cent, or $A2 billion of Australia's overseas earnings.

Australia's concern with agricultural protectionism throughout the world is heightened by the declining importance of wool in her exports. The severe price fall for wool has meant that Australian rural exports are becoming increasingly dependent on products such as wheat and grains, sugar, dairy products and meat and it is in precisely these areas that Australia's comparative advantage is most frustrated by the restrictive commercial policies of her trading partners.

In addition, the extent and seriousness of the current rural crisis has created a large welfare problem, not only among farmers but in the rural communities and industries which depend on a healthy agriculture. Although adjustment has been occurring continuously in Australian agriculture, unfortunately the pace of adjustment has not been fast enough. The recent sharp falls in farm incomes underline the urgent need for a faster flow of labour out of agriculture and the reorganisation of uneconomic units. Moves to assist this process have begun. This adjustment inevitably carries with it the need to develop policies of planned decentralisation to assist the adjustment of affected rural towns.

Australia's future economic growth depends on healthy international accounts. A real rate of growth in Australia's G.N.P. of 5-6 per cent in future years will require rising imports of goods and services and without

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[14] Australian sugar production has already been limited by quota restrictions to ensure the viability of the International Sugar Agreement. The EEC is not a signatory to this agreement.

[15] Commonwealth Bureau of Census and Statistics, *The Labour Force 1970*, Canberra.

[16] Commonwealth of Australia, *National Income and Expenditure 1970-71*, Budget Papers, August 1971.

the strong base provided by farm export earnings, such a rate of economic growth will be difficult to sustain without a sharply increased further dependence on the inflow of foreign capital.[17] Some observers are uneasy about such a prospect.

There is no question that some further structural adjustments must take place in Australian agriculture, but the extent, pace, and cost of these adjustments will depend on Australia's assessment of the overall world farm trade outlook and on her ability to gain increased access to overseas markets. This of course is a function of the negotiating willingness of Europe, Japan, and North America as well as Australia's own ability and willingness to negotiate.

As far as most of the developing countries are concerned, food consumption is low, but then so are incomes, and while the potential for increased demand for farm products is large, the scope for imports is limited due to the scarcity of foreign exchange. In addition, technological advance has already made an impact on imports in these countries and it is in their interests to encourage domestic food production leaving scarce foreign exchange for imports that are vital for development. No one can seriously criticize India, Pakistan and other less developed countries for seeking ways and means of raising their agricultural productivity and output.[18]

The one country that is not so neatly categorised and which has emerged as a major market for agricultural exporters increasingly frustrated by the protectionist excesses of Europe and the United States, is Japan. A developed, highly industrialised country where incomes are growing at a rapid rate and yet where food consumption is still relatively low, Japan has a huge potential as a market for farm products and thus has a vital role to play in any expansion in agricultural trade.

2. Japan's Agriculture and Trade Policy[19]

2.1 Inefficiency and Price Supports in Japanese Agriculture

Although Japan is about 80 per cent self-sufficient in food production, her agriculture, which produces a wide range of products, has suffered over the years from the fragmented nature and very small size of farms. Average farm size today is about 2.7 acres or a little over one hectare. This situation has persisted despite a massive exodus of labour from the farm sector over recent decades. A major reason for this has been a desire of farmers that land remain within the family even though members may work outside agriculture. In 1969, 80 per cent of Japanese farmers were part-time farmers earning about 58 per cent of their income from off-farm jobs.[20]

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[17] See J. G. Crawford 'Economic Prospects for Australia and its Neighbours', paper given at the *Cook Bi-Centenary Symposium*, Sydney, May 1970, paras. 8-9.

[18] See Sir John Crawford, *Agriculture in Development: The Australian Case and Some Contrasts with Developing Countries*, National Bank of Egypt, Fiftieth Anniversary Commemoration Lectures, Cairo 1971, Lecture II.

[19] Monetary values in this section have been converted to United States dollars at the rate of $US1 = 360 Yen.

[20] Ministry of Agriculture and Forestry, *Statistical Report, 1969-70*, Tokyo (in Japanese).

Between 1955 and 1970 the proportion of the workforce engaged in agriculture declined from 40.2 per cent to 18.2 per cent and it is expected to fall to around 12 per cent by 1975.[21]

Since the mid-fifties Japan's overall agricultural production has increased by about 60 per cent, mainly due to increases in rice and livestock products (see Appendix 8) but the scarcity of farming land and minute farm size have prevented farmers from taking full advantage of modern equipment and technology. In contrast to land productivity, labour productivity in Japanese agriculture is very low. In 1969, although employing almost one fifth of the workforce, agriculture accounted for only 6.5 per cent of net domestic product.[22]

The dominant product of Japanese agriculture is rice. In 1969, it accounted for over 40 per cent of the total value of agricultural production.[23] While about 70 per cent of Japanese agriculture requires either direct or indirect subsidy, the price support program for rice is by far the most extensive and costly of all the subsidisation schemes. It is important because it highlights the apparent attitude of the authorities in Japan toward domestic agriculture.

Originally a wartime measure, the Food Control Law (1942) empowered the government to exercise strict control over the supply and demand for food, in particular, rice. The Food Agency of the Ministry of Agriculture and Forestry purchases rice at a price sufficient to cover the cost of production and provide labour with an income comparable with that of non-farm workers.[24] Thus the producer price for rice has been raised each year in step with the rises in prices and non-farm incomes and it doubled between 1960 and 1969. This policy stimulated production to over 14 million tons per annum and in conjunction with a decline in consumption of rice, a stockpile accumulated, amounting to over 7 million tons in 1969, an amount greater than total world trade in rice in that year. The annual surpluses at that time were running at about 2 million tons.

In 1969 the deficit in the Foodstuff Control Account attributable to rice dealings was almost $US1.0 billion.[25] To combat this heavy drain on finances the government recently embarked on a program to cut the rice stock and reduce the annual output of rice to levels more in line with consumption. To this end the producer price of rice was held constant in 1969 and 1970 and an incentive payments scheme has been adopted to divert land from rice production. This has met with some success, and in 1970 the area planted to rice was reduced by about 10 per cent, and rice output fell by 1.3 million tons to 12.7 million tons.[26] But due to the dramatic decline in consumption (down from 118.3 kg. per head in 1962 to 96.9 kg. per head in 1969) even this reduced harvest has added to the stockpile.

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[21] Japan Economic Research Centre, *Japan's Economy in 1975*, Tokyo, March 1970. This proportion is still high compared with other developed country levels, eg: In 1965, Canada 9%; U.S.A., 6%; U.K., 4%; Australia, 10%; N. Z., 12%; Germany, 8%; France, 16%; see F.A.O., *The State of Food and Agriculture*, 1970, Rome.

[22] Ministry of Agriculture and Forestry, *op. cit.*

[23] *ibid.*

[24] Kenzo Hemmi, *Japanese Agriculture, 1968*, Department of Agricultural Economics, University of Tokyo, 1968.

[25] Food Agency, Ministry of Agriculture and Forestry, *Foodstuff Control Statistical Year Book*, Tokyo, 1970.

[26] Ministry of Agriculture and Forestry, *op. cit.*

In a further move to reduce the stockpile, some rice that has deteriorated in quality is being used as animal feed. More importantly, not only has Japan now ceased to be a major importer of rice, she has entered the rice trade as a large exporter. In 1970 Japan's exports of rice were 600,000 tons valued at $US164 millions.[27] The bulk of these exports were on credit terms to South Korea ($US110 million), Pakistan ($US26 million), and Indonesia ($US22 million). Thus in 1970 Japan's rice exports were running at half the level of Thailand, an important South East Asian rice exporter and a country with a growing trade deficit and which is dependent for 75 per cent of its export income on agricultural commodities. In 1969, Thailand's rice exports fell by 4 per cent to 1.026 million tons, well below their forecast level, and in addition, the value of these sales was down about 20 per cent due to a decline in prices.[28]

Price support schemes are also operated for a number of other crops including wheat, barley, soybeans, potatoes, rapeseed, sugar beet, silk, and tobacco.

In 1961 a Livestock Price Stabilisation Law became effective, and now buffer stock schemes are operated for livestock products. Subsidies are granted to milk and egg producers via systems of guaranteed prices.

None of the above support programs is on as large a scale or as costly as that for rice but an indication of the degree to which producer prices are supported in Japan is given in Table 1.

TABLE 1

PRODUCER PRICES OF AGRICULTURAL PRODUCTS IN MAJOR COUNTRIES, 1968-69

$US per 100 kg.

	Japan	France	West Germany	Italy	U.K.	U.S.A.	Australia
Wheat	15.40	8.76	9.76	10.76	6.43	4.56	5.10
Rice[a]	29.40	—	—	13.06	—	10.78	6.30
Barley	12.40	8.02	9.24	9.58	5.93	4.13	4.74
Cattle[b]	112.90	65.85	62.88	70.48	44.35	51.59	36.13
Pigs[b]	77.00	73.41	62.53	62.08	45.19	41.01	39.83
Poultry[b]	57.30	75.17	48.00	139.21	38.58	31.53	n.a.
Eggs	52.20	59.06	75.75	70.29	57.44	49.83	66.34
Fluid milk	12.90	8.42	10.10	10.82	8.56	11.57	7.18

[a] unhulled;
[b] liveweight;
n.a. not available

Source: Economic Planning Agency, *Economic Survey of Japan, 1969-70*, Tokyo, 1970, p. 87. The Australian figures have been calculated from data published by the Commonwealth Bureau of Census and Statistics and the Bureau of Agricultural Economics, Canberra.

[27] It is interesting that it was only in 1965 that her rice *imports* were valued at $US145 millions.

[28] United States Department of Agriculture, Economic Research Service, *The Agricultural Situation in the Far East and Oceania: Review of 1969 and Outlook for 1970*, Washington, p. 33.

Despite the high prices paid for wheat and barley, production has declined quite significantly over the past decade. In most other cases however, the high support prices have given rise to increased production, but the small size of farms resulting in low labour productivity and high costs, despite very high yields per acre, necessitate the continual upgrading of support prices to prevent the differential between farm and non-farm incomes from widening too far.[29] In addition to the high budgetary costs of agriculture the costs borne by consumers in the form of higher prices are considerable. In 1968 the domestic price of wheat was twice the average c.i.f. import price and the average ratios for some other products were rice (1967) 2.0; soybeans, 1.6; beef, 2.4; and butter 2.7.[30]

2.2 Japanese Imports

Although the volume of agricultural production in Japan increased by almost 40 per cent between 1960 and 1969, imports of agricultural commodities also rose strongly throughout this period, from $US1.7 billions in 1960 to $US4.2 billions in 1970. The value of imports of foodstuffs (including feedgrains) grew at about 16 per cent per annum, compared with 10 per cent for agricultural imports as a whole. The biggest increases among the foodstuffs have been in meats, imports of which have increased tenfold from $US14.2 millions to $US145.2 millions, fruits and vegetables up from $US33.3 millions to $US309.3 millions and cereals $US291.1 millions to $US1,048.9 millions (see Table 2). Although the composition of farm imports has changed quite noticeably over the last decade with foodstuffs now accounting for 53 per cent of the total compared with only 32 per cent in 1960, the market shares held by the major suppliers have remained fairly steady (Table3).

The United States is still by far the biggest supplier of farm products to the Japanese market. Imports from the United States in 1970 amounted to $US1.4 billions or 32.3 per cent of the total, a slightly larger share than in 1960. The United States is the major supplier of wheat, maize, sorghum, lemons, dried vine fruit, pork and oilseeds and a leading source of cotton and a multitude of other minor commodities.[31]

The second biggest individual supplier of farm products to Japan is Australia, although her share of the market fell slightly from around 15 per cent in 1960 to 13 per cent in 1970. This fall was due to the decline in wool prices throughout the sixties. The value of Japan's imports of agricultural products from Australia, excluding wool, doubled between 1964 and 1970. Australia is the leading source of Japan's greasy wool imports accounting for over 80 per cent of their total value. In addition Australia accounts for 80 per cent of Japan's beef imports and is a major supplier of wheat, barley, mutton and lamb, cheese, egg pulp, and sugar.

Imports from Asian countries in 1970 were $US808 millions and although double their level of a decade earlier have not grown as fast as total

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[29] Labour accounts for about 50 per cent of the cost of production of rice. This intensive use of labour has a dramatic effect on costs especially in view of the fact that good farm labour is now very scarce due to the movement of large numbers of young people out of agriculture.

[30] Economic Planning Agency, *op. cit.*, p. 88.

[31] Appendix 9 shows the leading suppliers of a number of major commodities, for selected years.

TABLE 2

COMPOSITION OF JAPAN'S AGRICULTURAL IMPORTS[a]

SITC Group	1960 $USm	1960 %	1970 $USm	1970 %
00 Live animals	0.5	0.0	16.4	0.4
01 Meat and meat preparations	14.2	0.8	145.2	3.4
02 Dairy products and eggs	17.2	0.9	49.4	1.2
04 Cereals and cereal preparations	291.1	16.5	1,048.9	24.7
05 Fruit and vegetables	33.3	1.9	309.3	7.3
06 Sugar and sugar preparations	121.2	6.9	346.3	8.2
07 Coffee, Cocoa, Tea, etc.	24.0	1.4	153.3	3.6
08 Animal feedstuffs	17.8	1.0	136.2	3.2
09 Miscellaneous foodstuffs	2.5	0.1	3.9	0.1
11 Beverages (ex. distilled alcoholic)	13.6	0.8	65.5	1.5
121 Unmanufactured tobacco	13.6	0.8	65.5	1.5
21 Hides and skins	41.4	2.4	102.3	2.4
22 Oilseeds, nuts, and kernels	187.4	10.6	542.1	12.8
231.1 Natural rubber	143.0	8.1	129.5	3.0
261-265 Natural fibres	757.3	43.0	957.0	22.6
29 Crude animal and vegetable materials	22.6	1.3	90.5	2.1
4 Oils and fats	38.0	2.2	78.3	1.9
555.1,599.5 Essential oils, casein, albumen, etc.	32.3	1.8	49.2	1.2
Total	1,762.9	100.0	4,239.7	100.0

[a] c.i.f., calendar years.

Source: Ministry of Finance, *Japan Exports and Imports: Commodity by Country*, Tokyo, 1961 and 1971.

TABLE 3

JAPAN'S AGRICULTURAL IMPORTS BY MAJOR SOURCES OF SUPPLY[a] [b]

	1960		1965		1970	
	$USm	%	$USm	%	$USm	%
United States	545.1	30.9	973.4	34.3	1,367.7	32.3
Canada	121.0	6.9	147.1	5.2	224.5	5.3
Asia[c]	401.3	22.8	694.1	24.5	808.8	19.1
Australia	266.9	15.1	387.6	13.7	541.2	12.8
New Zealand	22.2	1.3	48.9	1.7	99.5	2.3
Latin America	244.8	13.9	362.1	12.8	593.7	14.0
EEC	17.0	1.0	37.0	1.3	88.7	2.1
Other	144.6	8.1	185.3	6.5	515.6	12.2
Total Agricultural Imports	1,762.9	100.0	2,835.5	100.0	4,239.7	100.0
Agricultural Imports as Percentage of Total Imports	39.2		34.7		22.5	

[a] For composition of agricultural imports see Table 2.

[b] c.i.f., calendar years.

[c] Includes India, Pakistan and Middle East to the east of the Suez Canal in addition to South East Asia including China.

Source: Ministry of Finance, *Japan Exports and Imports*, Tokyo (various issues).

agricultural imports. Thailand is a large supplier of maize; Taiwan, pork, bananas, and sugar; the Ryukyus, sugar; China, soybeans.

As a group the Latin American countries have a share of 14 per cent in the Japanese market. Argentina is a leading supplier of maize and sorghum; Brazil, Nicaragua and Mexico, cotton and Ecuador dominates the large market for bananas.

The major products supplied by Canada are wheat, barley and oilseeds. Although imports from Canada doubled over the decade, her share of the overall farm product market fell to 5.3 per cent.

Both New Zealand and the EEC still only hold a small share of the market, but imports from both sources have expanded quite rapidly over recent years, with New Zealand being a major supplier of wool, mutton and dairy products, and the EEC having a significant impact with its subsidised exports on the barley and dairy products markets.

2.3 Japan's Import Restrictions

Even though agricultural imports have grown, the rate of growth has been held in check by the Japanese government which maintains a comprehensive system of import restrictions, including quantitative controls, state trading operations, tariffs and 'administrative guidance'. It is, of course, within the framework of these restrictions that Japan administers her agricultural policies.

By 1965 import restrictions not consistent with the provisions of GATT had been removed on nearly all major non-agricultural items and on some important agricultural products such as maize, soybeans, grain sorghum, and hides and skins. However, agricultural commodities are among the most important still subject to quantitative import restrictions. At the beginning of 1971, 123 items were either subject to quantitative restriction or state trading. Of this group 80 items were under quantitative restrictions which were inconsistent with the GATT articles. By June 1971 the number had been reduced to 60 and it is anticipated that by the end of the year (1971) only 40 items will remain under residual import restriction.[32] This latter group still includes 28 agricultural items, the major ones being, beef and veal, ham and bacon, processed cheese, flour, fresh oranges and fruit juices.

At present there are 43 items, whose import is restricted, but for which the Japanese government claims sanction under GATT Articles, XVII, (State Trading) and XX, XXI, (General and Security Exceptions). The agricultural products whose importation is controlled completely by the state trading organisations are rice, wheat, barley, tobacco and most dairy products including butter and condensed and powdered skim and wholemilk. Unprocessed cheese, casein and lactose are not quantitatively restricted.

In addition to the quota restriction on beef and veal, imports attract a tariff of 25 per cent and an additional levy of up to 10 cents per pound. Imports of pork incur a tariff of 10 per cent, whilst mutton and lamb imports, although not quantitatively restricted, attract a tariff of 7.5 per cent.

Tariff rates on agricultural items are not generally very high. Raw materials such as wool, hides and skins are free, as are grain sorghums and meat and fish meal for animal feed. In general the higher the degree of processing, the higher the tariff. For example tariffs on canned fruits range up to 55 per cent. However, for processed cheese, butter, beef and veal, wheat, and a number of other items the protective effect is due to the quantitative restriction and tariffs are not an important barrier.

In the case of sugar, imports are controlled by the Sugar Corporation, and all imports are subject to a levy to bring the price up to the minimum import price, then a surcharge to raise it to the target price. On top of this a tariff is collected and a heavy consumption tax is placed on refined sugar.[33]

Administrative guidance which is an important technique of trade regulation, is used in Japan as an additional weapon to control the flow of imports of particular commodities that may be causing discomfort to domestic producers. For example, in 1968 imports of eggs (mainly frozen pulp) were voluntarily restricted by importers at the suggestion of the Ministry of Agriculture and Forestry which was under considerable political pressure from domestic egg interests. The effective use of this technique removes the grounds for the implementation of more visible protective measures such as increased tariffs or quotas, and to that extent lessens the prospect of retaliation although the protective effect may be equally severe.

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[32] Ministry of International Trade and Industry, *Bulletin No. 6260*, Japan, September, 1970.

[33] The tariff on imported raw sugar is $US104 per metric ton. This compares with an average c.i.f. import price of $US105 per metric ton in 1970. The consumption tax on refined sugar is $US48 per metric ton.

2.4 Changing Consumption Patterns and Food Prices in Japan

Despite these protectionist policies Japanese agricultural imports have risen strongly over the last decade. Half of these imports now consist of foodstuffs and animal feeds, and underlying this import growth is a significant change in the level and structure of demand for foodstuffs in Japan.

The structural transformation of the Japanese economy, bringing with it rapidly increasing per capita incomes has resulted in quite radical changes in the food consumption patterns of the people. As incomes and living patterns have changed there has been a substantial improvement in the variety and nutritional value of the food intake (see Appendix 10). From the mid-fifties to 1969, per capita consumption of rice, barley, and potatoes decreased significantly, while per capita intake of meat, eggs, dairy products, fruit, vegetables, sugar and fish all increased. These changes resulted in the average daily calorie intake increasing from 2240 in 1955 to 2447 in 1969. Over this period the contribution of starchy foods to total daily calorie intake fell from 74 per cent to 56 per cent while that of livestock products increased from 6 to 12 per cent, and fruit and vegetables from 4 to 6 per cent. Also in 1969 the average daily per capita intake of protein was 75.1 grams, an increase of 9.0 grams over the 1955 level. Significantly this increase was made up wholly of animal protein.

However, despite this substantial improvement in diet, the per capita protein and calorie intake is still well below the levels in other developed countries as well as some less developed countries (see Appendix 11). In view of the fact that national income per capita in Japan in 1970 was equal to that of the United Kingdom, and growing rapidly, it can be argued that a good deal of the explanation for the relatively low level of nutrition in Japan can be found in the extremely high food prices that prevail. This is reinforced by the fact that the saturation rates for such consumer durables as washing machines, radios, and colour television, are among the highest in the world.

Not only are food prices in Japan very high, they are rising at a rapid rate. Between 1965 and 1969 price rises for foodstuffs on average accounted for 42 per cent of the annual increase in consumer prices of 4.9 per cent (see Appendix 12). The largest rate of increase in prices over this period occurred with foodstuffs under state trading (e.g. rice, wheat, dairy products) which rose at an annual average rate of 7.1 per cent. Interestingly the rate of increase in the prices of non-liberalized food items was only slightly greater, at 4.9 per cent, than that of liberalised food items, 4.6 per cent, indicating the degree to which import quotas have been raised each year to keep prices down. Imports of beef, which are restricted by quota, increased from 6,200 tons in 1964 to 23,227 tons in 1970. Similarly the flow of imports of pork is varied in order to contain domestic price rises.

In 1970 the consumer price index rose 7.7 per cent, the sharpest yearly rise since the Korean war. Contributing to this overall price increase were price rises in vegetables 33.2 per cent, fruits, 22.1 per cent, and fish 20.6 per cent.[34] Similar price rises in these commodities occurred in the previous year, and the effects can be seen clearly in Appendix 10; per capita consumption of fruit, vegetables, and fish, the major sources of protein in the Japanese diet, fell significantly after a sustained increase since the mid-fifties.

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[34] *Statistical Bureau*, Prime Minister's Office, Tokyo.

2.5 Trends in Japanese Consumption, Production and Imports

In Japan in 1969 80 per cent of actual food consumption was home produced. This level was slightly below the levels ruling earlier in the decade and has been declared the desired target ratio.[35] In keeping with this attitude the Japanese Ministry of Agriculture and Forestry recently prepared some projections of supply and demand of agricultural products in 1977.[36] These projections imply the continuation of the present policies toward agriculture in Japan, and indicate that the ratio of domestic production to consumption for most products in 1977 will be similar to 1969 levels (see Appendix 13).

One of the most potentially significant declines in the ratio of home production to consumption has occurred in meats. As a whole the ratio declined from 94.6 in 1963 to 82.9 in 1969, while for pork and chicken the ratios fell from 100.0 in 1963 to 93.6 and 95.5 respectively in 1969, and that of beef was down from 97.5 to 92.7. The lower overall ratio was brought about in large measure by the increased consumption of mutton which is almost wholly imported.

The projections indicate a continuation of the trend away from the consumption of starchy foods towards a higher per capita intake of animal products, vegetables and fruits. In order to maintain the overall 80 per cent self-sufficiency ratio in the face of such dietary changes, changes in the emphasis of domestic production will be required. Under government encouragement the focus of domestic production will be shifted away from rice toward the increased production of meats, dairy products, eggs, vegetables and fruits. To this end, an acreage diversion program for rice has been introduced, and increased production of meats and dairy products is being assisted by such measures as legislative action to achieve larger farm size, land and stock improvement schemes, and price support policies maintained within the comprehensive framework of import restrictions.

The table below compares the projected 1977 per capita consumption and production of a number of food groups with their 1969 levels.

The most significant changes in per capita consumption levels are expected to occur in fruits and livestock products which are expected to increase by over 60 per cent compared to their levels in 1969. However, due to the influence of population growth, estimated at 1.2 per cent per annum, total consumption will increase at a faster rate. In order to maintain the desired levels of self-sufficiency, production will have to increase at the same rate as total consumption and these increases are shown in the above table. Some idea of the extent of the required increases in production can be gauged from the past growth rates. For example, over the eight years 1962 to 1969, beef production increased by 67 per cent, pork by 81 per cent, and milk by 85 per cent. Clearly, to achieve the 1977 target levels of production these rates of growth will have to be maintained over the next eight years. But owing to the acute shortage of land, labour, and the very small size of farms such production increases will only be achieved at a very high cost, adding further to the already severe inflationary pressures in the economy.

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[35] Ministry of Agriculture and Forestry, *Annual Report on Trends in Agriculture, Parts I and II*, Tokyo, 1970 (in Japanese).

[36] Ministry of Agriculture and Forestry, *Long Term Projection of Supply and Demand for Agricultural Products*, Tokyo, 1968 (in Japanese).

TABLE 4

PRODUCTION AND CONSUMPTION OF SELECTED FOOD GROUPS: JAPAN

	Consumption (Kg. Per Capita Per Annum)			Production (Thousand Metric Tons)		
	1969	1977	Percentage Change	1969	1977	Percentage Change
Rice	96.9	91.6	-5.5	14,003	12,442	-11.1
Wheat	31.3	32.9	+5.1	758	795	+4.9
Barley	2.2	1.4	-36.4	812	902	+11.1
Soybeans[a]	5.6	5.8	+3.6	136	121	-11.0
Vegetables	120.1	127.5	+6.2	15,507	17,447	+12.5
Fruits	36.6	62.0	+69.4	5,162	9,725	+88.4
Dairy products	47.3	78.3	+65.5	4,574	8,099	+77.0
Meats[b]	10.9	18.4	+68.8	1,190	2,300	+93.3
Eggs	12.6	14.8	+17.5	1,523	1,907	+25.2

[a] Per capita figure refers to use as food only.

[b] Excluding whale meat.

Source: Ministry of Agriculture and Forestry, *Food Balance Sheet, 1969*, Tokyo; Ministry of Agriculture and Forestry, *Long Term Projections of Supply and Demand for Agricultural Products*, Tokyo, 1968, (in Japanese).

Even if this projected growth in farm production is attained, imports of these commodities will have to grow at the same rates. In addition, imports of animal feedstuffs such as feedgrains and supplements will have to grow enormously to sustain the projected growth in domestic production of livestock products. For example, Japan's imports of feedgrains increased from 4.7 million tons in 1964 to 10.7 million tons in 1970 in order to sustain the increase in domestic meat production over that period.

At these projected production, consumption, and import levels in 1977, per capita calorie intake in Japan should be 2,664, with a total protein intake of 85.8 grams of which 39.5 would be of animal origin. Thus the projections suggest that despite the increases in production and imports, the average level of nutrition in Japan, although improved, would still be below all other developed countries and this would be at a time when Japanese G.N.P. per capita is expected to be among the highest in the world.[37]

The picture that emerges is one of an inefficient agriculture by world standards in terms of cost per unit of output, already under considerable pressure from growing demand brought about by the rapid growth in incomes. Even if the current import restrictions remain, imports are likely to grow quite substantially and if liberalisation proceeds, imports of products such as meats and dairy products with high income elasticities, as well as animal feedgrains, will increase at an even faster rate.

[37] Projections indicate that by 1985 Japan's GNP per capita will exceed that of the United States and Sweden and be the highest in the world; Japan Economic Research Centre, *The Japanese Economy in 1985*, Tokyo, 1971 (in Japanese).

There is considerable pressure, from both internal and external sources, for further liberalisation of import restrictions. Not only are many of the import restrictions inconsistent with the GATT articles, the scope for imports to reduce the severe inflationary pressures in the economy is recognised by the forces against agricultural protectionism led by the urban consumers and big business which produces for the international market. In addition, the issue of agricultural protectionism is already important and likely to become more so as Japan's need to secure her exports market grows.

The combination of an inefficient domestic agriculture requiring heavy price support and substantial protection from imports, coupled with a large population with a relatively low level of nutrition, yet with high and rapidly growing incomes, has given rise to strong demand pressures that scarce domestic resources are unable to satisfy. As in the past, these pressures could be expected to limit the scope of protectionist forces and thereby give rise to further increases in food imports. In the absence of any liberalisation of residual import restrictions such import growth would come about through further relaxation of import quota limits and a more liberal attitude on the part of state trading authorities. Failing relaxation some inflation of prices of available supplies must be expected.

3. The United States, Canada and New Zealand and the Japanese Market

3.1 Exports to Japan

The United States, Canada and New Zealand share Australia's interest in the growth of the Japanese market because all are being adversely affected by those factors governing world trade in agricultural products which have already been outlined in respect of Australia.

Japan is an important market for the agricultural products of the United States, Canada and New Zealand as well as for raw materials and manufactured goods (Appendix 14). In 1969, United States agricultural exports of $US1,300 millions to the whole of the Common Market accounted for 21 per cent of her total agricultural exports. Outside the EEC, the largest market for United States' farm products was Japan. In 1969, the United States exported agricultural produce worth almost $US1 billion to the Japanese market, with the major products being soyabeans ($US200.3 millions), maize ($US190.6 millions), wheat ($US119.3 millions) and other feed grain, mostly sorghum $US88.4 millions). Other significant United States agricultural exports to Japan were cattle hides, cotton, tobacco, lucerne (alfalfa) meal, inedible tallow, pork, lemons and limes, plus a host of other smaller items (Appendix 15). Apart from sales to the EEC and Japan, the United States also exports large quantities of farm products to Canada, United Kingdom, 'Other Asian' countries[38] and Latin America. Between 1965 and 1969, United States exports to Japan increased by about $US50 millions and to Canada by $US93 millions whereas over the same period, the value of her exports to the EEC and the United Kingdom declined.[39]

[38] About three quarters United States total agricultural exports to 'Other Asian' countries 1954-55 to 1967-68 was under specified government programs.

[39] In 1970 United States agricultural exports $US1,559 million to the EEC reached record levels mainly because exports of oilseeds, which are not subject to variable levies, rose by $US155 millions from the 1969 total of $US500 millions. (US D. of A. *Foreign Agricultural Trade of the United States*, March 1971).

Japan is the third largest individual market for Canadian agricultural products, and in 1969 Canada's farm exports to Japan, at $US137 millions, accounted for 12 per cent of her total agricultural exports which had declined by 20 per cent between 1965 and 1969 to $US1.2 billions. Canada's major exports to Japan in 1969 were wheat ($US70.5 millions), and oilseeds ($US39.8 millions).

New Zealand's agricultural exports to Japan in 1969 were valued at $US79 millions, up from $US44 millions in 1965. Japan ranked as the fourth largest New Zealand market for agricultural products, after the United Kingdom, United States and the EEC. In 1969, the United Kingdom and EEC together accounted for three fifths of New Zealand's agricultural exports. New Zealand's main exports to Japan are meat, dairy products and wool.

As with Australia and the United States, agricultural exports from Canada and New Zealand to the United Kingdom and the EEC declined between 1965 and 1969. In the case of Canada the decline was from $US512 millions to $US381 millions and of New Zealand from $US619 millions to $US605 millions.

The interests of these agricultural exporters in the Japanese market differ significantly. They depend not only on actual sales to Japan but also on the importance of agriculture in each economy[40] and on the importance of agricultural exports for that economy (Appendix 16).

In 1969, exports of agricultural products from the United States accounted for 16 per cent of total merchandise exports, down from 23 per cent in 1965. Although agriculture provides a small and declining share of the United States gross domestic product and there have been spectacular decreases in both numbers of farms and numbers employed in farming in recent years, the United States still has a farm employment of about 4.5 million[41] (about 4 per cent of employment) on 3 million farms. Agriculture remains a significant source of regional employment and farmers are united in well run organisations which the government cannot disregard.

Canada has a rapidly growing domestic market for agricultural products which takes a greater share of production than the export market, even of wheat and oilseeds.[42] Agricultural exports accounted for 18 per cent of total exports in 1965 and only 8 per cent in 1969 but in 1968 agriculture employed 546,000 on 430,500 farms.[43]

In New Zealand where in spite of successfull efforts at diversification[44] agricultural products still account for about 85 per cent of total

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[40] Percentage GDP originating in agriculture (IBRD)

	US	Canada	New Zealand
1965	3.4	6.5	15.3
1968	2.9	5.9	15.4

[41] US Government Printing Office, *Economic Report of the President*, together with the *Annual Report of the Council of Economic Advisers*, p. 293, (Washington, 1971).

[42] T. S. Rackham, World Agricultural Trade and Merchandising Opportunities in the 1970s in *Canadian Journal of Agricultural Economics*, Vol. 18, No. 1, Feb./Mar. 1970.

[43] Canada, Dominion Bureau of Statistics, *Yearbook 1969* Statistics Canada *Canadian Statistical Review*, August 1971 gives an average monthly employment for 1970 of 511,000 and a labour force of 524,000.

[44] New Zealand exports of timber and timber products and of manufactured goods increased rapidly in the 1960s. A. R. Frampton, *Reconstruction and the Use of Financial Incentives in New Zealand Rural Industries;* paper given at 43rd ANZAAS Congress, Brisbane, May 1971, Table 2.

exports, the position is quite different. In 1968 there were 66,866 farms. Farming now employs about 11 per cent of the workforce[45] (about 126,000).

Moreover, the interest of these agricultural exporters is related not only to their present but also to their potential sales to Japan. As with Australia all could produce economically and without difficulty more of the major items they now sell to Japan. Both Canada and the United States have severely restricted acreages of grains and other field crops. In 1969, New Zealand one of the most efficient producers of dairy products in the world introduced a dairy beef diversion scheme[46] to encourage farmers to change over to meat production.

3.2 Effects of the Entry of the U.K. into the EEC

Despite the contraction of the United Kingdom market throughout the sixties, agricultural exports of all three countries to this destination were still large in 1969. The United States exported agricultural products valued at $US376 millions, Canada and New Zealand accounted for $US239 millions and $US461 millions respectively. The entry of the United Kingdom into the Common Market must therefore greatly influence the future trade policies of all three countries.

For Canada, as for Australia, not only loss of British preferences but adjustment to British entry into the EEC must be faced immediately. In 1969, wheat made up about one third of total Canadian agricultural sales to the United Kingdom. Prospects for Canadian wheat are uncertain but the British market for Canadian cheese and tobacco are at considerable risk. Canadian reliance on the three major markets of the United States, United Kingdom and EEC which together took 70 per cent Canadian agricultural exports in 1969, must create problems of adjustment, bearing in mind the potential production of an enlarged EEC offering higher prices to British farmers and continuing incentives to those engaged in farming within the present Common Market.

Although the United States has large sales to the Common Market these are increasingly concentrated in non-variable levy items such as oilseeds and animal feeds other than grains. In 1969, United States sales of foodstuffs to the United Kingdom were about the same as Canada's ($US160 millions) though sales of agricultural raw materials including tobacco were more than twice Canada's. Since it is food items which the EEC's variable levy system mainly affects, United States exporters of grains, dairy products and meats must share Canadian concern about exports of these items. Restrictions on imports of fruits and vegetables, the inclusion of tobacco in the CAP and the fact that over 90 per cent of EEC farm production[47] is now covered by CAP, together increase these anxieties.

The trade displacement which must result from United Kingdom entry will affect New Zealand gradually and New Zealand's eventual trading alignment may well depend on how difficult she finds it to obtain alternative markets in the Pacific. New Zealand may find that higher prices are no compensation for reduced quantities sold to an enlarged EEC and that the EEC

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[45] ANZ Bank *Quarterly Survey*, July 1971, pp. 22-3.

[46] Discontinued in 1970 at the request of Dairy Board on the grounds that drought had seriously affected milk supplies.

[47] J. van Lierde, Internal Aspects of EEC Agricultural Policies in *Proceedings of a Conference on Problems and Prospects in Atlantic and Continental Agricultural Trade*, (University of Guelph, Ontario, 27 September 1970).

undertaking to seek international agreement on dairy products may prove unproductive. Then, because of her need to export agricultural products, New Zealand may have to press (and pay) for closer trading relations with both Australia and Japan. Some agricultural exports to Australia could expand in return for concessions within the framework of the Australia-New Zealand Free Trade Agreement.[48] New Zealand has widened her range of agricultural products to include processed foods and made efforts to expand her agricultural exports to other markets but in Asian, Pacific Islands and Latin American markets there is strong competition from other efficient exporters in the region.

There is good reason to expect that with the continuance of the CAP in an enlarged EEC, competition for all available markets for temperate zone agricultural products will intensify.

3.3 Competition for the Japanese Market

Similar competition exists in the rapidly growing Japanese market (Appendix 15). Moreover, the EEC, itself a major importer of agricultural products, has since 1968 been competing strongly in the Japanese market with sales of wheat, barley, butter, dried milk and dried peas. The Canadians had to reduce barley prices to regain a share in the Japanese market after EEC sales of surplus barley in 1968 and 1969. The EEC also competes directly with the United States in items such as essential oils and lard though the United States has apparently regained its Japanese market for chickens at the cost of losing a market in Greece and Switzerland to the EEC.[49]

The United States, New Zealand and Canada all sell meats, dairy products, animal feeding stuffs, hides and skins and animal oils and fats to Japan. The United States and Canada are both prominent in the markets for cereals and oilseeds.

Competition within some broad commodity groups is limited. For example, Canada and the United States sell pork to Japan, New Zealand and Australia lamb and mutton. The United States supplies soyabeans and safflower, Canada linseed, mustard seed and rapeseed.

Competition is also limited in specialised items of processed foodstuffs. Here the market is dominated by a single supplier and the United States which has supplied a very large range of export goods to the Japanese market since the 1950's has a strong position.

The interests of the three major Pacific area exporters overlap those of Australia in areas such as wool, wheat, sorghum, oilseeds and lucerne meal in the Japanese market, and, in addition, there are commodities such as cheese, tobacco, casein and linseed in which the three exporters do not compete in the Japanese market but do so in the major markets of the EEC and United Kingdom (Appendix 5). These supplies could, if diverted to the Japanese market, increase competition there.

There are also items such as Canadian butter which are occasional exports and which could, as the EEC exports of surplus barley have shown, affect market prices. There is no doubt of the competition among suppliers

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[48] Under the Australia-New Zealand Free Trade Agreement New Zealand exports of agricultural products to Australia doubled in value between 1965/66 and 1969/70 and her trading position with respect to Australia improved. In 1970/71 the excess of imports from Australia increased but there was a general increase in New Zealand imports.

[49] European Community 7-8, July-August 1971, p. 8.

of a large number of products on the Japanese market and this seems certain to increase, even without deliberate action[50] on the part of those countries concerned, as possibilities of substitution increase with advances in food technology.

3.4 Agricultural Support Programmes

All three countries face the problem of decline in farm incomes compared with those in other sections of the community. All have taken steps to maintain and increase efficient production and marketing but their approaches have been different. In all the cost of agricultural support programs both direct and indirect rose steeply in the 1960s.

All three countries operate schemes of tariff protection for domestic agricultural production although in some cases there are seasonal duties.[51] In addition New Zealand has a complex system of import licensing introduced mainly for balance of payments reasons. The United States operates quotas under the Agricultural Adjustment Act to protect price support programs and under PL88-482 when meat imports are excessive. Canada requires import permits for some dairy products and licences for wheat, barley, oats and their milled products.

New Zealand has not needed to provide direct export subsidies for her agricultural products and her marketing schemes have operated successfully[52] with very little government assistance beyond provision of overdraft facilities by the Reserve Bank. The estimated cost of direct assistance to farmers in 1970-71 was $US39.2 millions and total government expenditure on agriculture was estimated at $US99.5 millions.[53]

Canada has used export subsidies sparingly (there is an export equalisation fund to cover exports of surplus dairy products) and supports prices both home and export through deficiency payments and purchase programs.[54] Canada seems to have solved the problem of temporary price supports by her scheme of mandatory support of a basic price which was originally 80 per cent of the average in a 10 year period. For the 10 year period to 1968, 22 products received support through the Agricultural Stabilisation Board at a cost of $US616.7 millions. These included meat, dairy products and grain originally scheduled and vegetables, fruit and poultry.[55]

Australia's expenditure on agricultural support and adjustment has risen rapidly. Estimated expenditure in the 1971-72 Budget was $US308 millions[56] as against actual expenditure in 1968-69 of $US193 millions. Two thirds of the increase and one quarter of the total was budgeted for assistance to the wool industry.

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[50] United States in the Agricultural Act of 1970 abandoned grain acreage control. Grain acreages in US increased in 1971. EEC farmers sowed more oilseeds

[51] Imports of fruits and vegetables to Canada and United States.

[52] The New Zealand Dairy Board to distribute $US6.7 millions to farmers in 1971. Reserve Bank of New Zealand *Bulletin*, June 1971.

[53] Frampton *op. cit.* pp. 9, 10. For 1969-70 actual expenditure was $US13.3 millions and $US66.3 millions respectively.

[54] B. Fernon. *Atlantic Trade Study, Issues in World Farm Trade* (Trade Policy Research Centre, 1970) p. 41.

[55] *Canada Yearbook 1969 op. cit.*

[56] In addition to assistance with fertilisers and petroleum products ($US82 millions), reconstruction schemes accounted for $US58 millions, stabilisation funds and bounties $US82 millions. Commonwealth of Australia *Budget Papers* Budget Speech 1971-72, and Statements attached to the Speech, (Canberra, 1971).

The United States has subsidisez agricultural exports extensively. The cost of direct export subsidies was $US162.9 millions in 1969-70 (in 1963-64 it was $US821.7 millions)[57] and domestic prices are also subsidised (wool to 0.72 cents a lb.). An estimated outlay of $US5,262 millions in fiscal 1971 for agricultural and rural development and $US5,804 millions in fiscal 1972 was allowed for in the US Budget.[58]

The extent and direction of subsidisation of production will be important negotiating issues among the Pacific agricultural exporters themselves. Collectively they have a strong common interest in negotiations with Japan. With Australia, both the United States and Canada are divided on the issue of free trade in agricultural commodities and New Zealand is working out the implications of its special position *vis-à-vis* the EEC. But all three countries, mindful of the importance of agricultural interests and in the face of rising production in the EEC, view a growing Japanese market as a solution to some of their problems and along with Australia they will continue to press for further liberalisation of Japan's agricultural trade policy.

4. Trade Policy Options

4.1 A Campaign Against Agricultural Protectionism

The case for a concerted attack on the problem of agricultural protectionism by industrial countries has perhaps never been more pressing. The entry of the United Kingdom into the EEC threatens to extend and strengthen European agricultural protectionism. The delicate balance of politico-economic forces in the United States, the agricultural interests in Canada, and the crucial role of agricultural exports in Australia and New Zealand provide the rationale for special initiatives from Pacific countries against the forces of agricultural protectionism. It is not in the interests of agricultural exporters to have agricultural trade excluded from the attempts, represented in the articles of GATT, to evolve rules for freer trade. They wish to negotiate and naturally look to Japan.

The success of any such initiatives must largely depend on the stance taken by Japan. The high rates of economic growth sustained in Japan and the scarcity of domestic agricultural resources have resulted in a strong growth in Japanese imports of foodstuffs and animal feeds over the past decade. This import growth is likely to continue, but as in the past, the rate of growth of food imports will be limited by the protectionist stance of the Japanese authorities toward a domestic agriculture that is inefficient by world standards. Pacific agricultural exporters, including the United States, have a strong interest in the Japanese import market. Here then is an area where a Japanese government can still offer substantial concessions in international negotiation, where it can involve the United States in a significant retreat from protectionism, and where it can demonstrate new leadership in trade policy in contrast to the inward-looking European Economic Community.

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[57] US D. of A. *Foreign Agricultural Trade of the United States*, February 1971, p. 10.
[58] US Executive Office of the President, Office of Management and Budget, *The US Budget in Brief, Fiscal Year 1972* (Washington, 1971) p. 36.

There are two levels on which the campaign against agricultural protectionism can be pressed. In the longer term, there is some prospect that ground can be gained, even against Europe, within GATT and other world forums. The special initiatives within GATT and the OECD Study Group on problems in agricultural trade should lead to a clearer specification of the magnitude of agricultural protectionism and the incentives to reduce it. These are worthwhile endeavours but they are unlikely to produce concrete results soon enough.

In the intermediate term, there is some promise of gaining ground in bilateral negotiations or regional negotiations among directly interested parties. Concessions on agricultural protectionism will have to be reciprocated with concessions elsewhere.

There is certainly scope for the negotiation of a new and major economic agreement involving Japan and Australia.

4.2 Factors in the Removal of Trade Barriers

Since 1957, when Australia and Japan signed an 'Agreement on Commerce', trade between the two countries has grown considerably. In 1970-71, Japan was Australia's largest export market and accounted for 27.1 per cent of total exports. Japan supplied 13.8 per cent of total Australian imports and was third largest supplier after the United States and United Kingdom. In 1970, Australia supplied 8.0 per cent of Japan's total import requirements and was her fifth largest export market after the United States, South Korea, Taiwan and Hong Kong, accounting for 3.1 per cent of total exports.

The Australia-Japan Agreement on Commerce was re-negotiated in 1963 and the full rights of GATT are reciprocated under this Agreement. Although trade between the two countries has grown markedly throughout the past decade or more and prospects for further growth within the current trading framework are bright, the potential gains from trade between Japan and Australia will not be fully realised without further mutual trading concessions. Any new economic agreement between the two countries would have to be consistent with the GATT articles. The prospect of costly retaliation by affected parties, consequent on a flouting of basic GATT principles, would be far too great a risk for both nations in comparison to the gains that would be made. This rules out any suggestion of a unilateral offer of tariff preferences confined to Japanese goods.

On the Australian side the flow of exports from Japan is inhibited by Australia's protective tariff. Almost one third of Australia's imports from Japan in 1969-70 attracted duties of greater than 30 per cent.[59] Perhaps this is an indication of Japan's competitive vigour; nevertheless, there is room for tariff cuts. More importantly, there is now no need to give preference to Britain on goods not produced in Australia and this preference could safely be removed on By-Law items and probably on most items with MFN rates of 10 per cent or less. The wider question of preference is touched on below.

Progress in the direction of scaling down these tariff barriers has been slow but recent years have witnessed a strengthening in the forces for change. For a number of years Australia was able to maintain a very low rate of unemployment whilst at the same time contain the rate of inflation.

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[59] Commonwealth Bureau of Census and Statistics, *Customs Clearances at Specified Rates of Duty: Australia, 1969-70,* Canberra, November, 1970.

Recently, however, the rate of inflation has accelerated and the role of Australia's tariff policy in this process has increasingly come under attack from agricultural interests, other industries producing for the world market, as well as urban consumers. The Australian Tariff Board has begun to review the role of the tariff in the Australian economy and reassess the very high levels of protection granted to some industries.

This process of review may prove rather slow. Moreover, the balance of political forces is such that significant modification of Australia's tariff is unlikely unless concessions are reciprocated by the major trading partners. This applies especially to the preferential tariff.

If Britain enters the EEC and even if she does not, Australia will need to restructure her preferential tariff system. At present under her trade treaty with Britain, Australia grants tariff preferences to British exports in the Australian market in exchange for preferred access to the British market. In this area three options are open to Australia; she could raise British Preferential Tariff (BPT) rates to the Most Favoured Nation (MFN) level, reduce MFN rates to the BPT level, either across the board, or selectively on commodities of particular interest to Japan and other trading partners prepared to negotiate. Alternatively compromise could be made with movements in both BPT and MFN rates on a selective basis.

It should be emphasised that there can be no presumption that Australia will make a unilateral tariff reduction. Although the political climate in Australia, at present, is much more favourable for an alteration in the tariff than in the past, such actions are internationally negotiable and the balance of forces in Australia is such that considerable gains would have to be in sight before any significant action outside the long process of Tariff Board review could be contemplated.

The rapidly growing Australian mineral industry, which is destined to play a key role in Australia's future economic growth, already has close ties with Japan; the bulk of Australian iron ore contracts for example are with Japanese firms. While Australian suppliers have real advantages in terms of quality, price and stability of supply, the adoption by Australia of a firm mineral development policy embracing both foreign investment in mineral exploitation and processing could go a long way toward reducing any uncertainties and make for a closer understanding between the two nations. Progress toward more joint ventures in mineral processing in Australia, for example, would be welcomed by both Japan and Australia. Certainly, any new economic agreement involving Japan and Australia would have to encompass both countries' interests in foreign investment and resources development. In addition, it is imperative that both countries keep in mind the position of mineral exporters in the less developed countries, and press for the development of processing industries in these countries.

On the Japanese side, Japan's protective policies toward her agriculture are a major bone of contention with Australian producers, now under considerable pressure from rising costs and falling world prices for traditional lines of specialisation. New lines of agricultural specialisation appear profitable, but readjustment is costly. If expansion is limited by severe protectionism in importing countries, the necessary investment for new land uses may well be discouraged. Many of Japan's protective policies are residual import restrictions which are quite inconsistent with the articles of GATT and Australia, along with other countries, will continue to press for their unilateral removal. The remaining barriers in the Japanese market are state

trading policies which have the same effect as quantitative restrictions, and, although the state trading authorities do not necessarily discriminate between suppliers on other than normal commercial grounds, these practices, by their secretive nature, encourage accusations of discriminatory treatment.

Australian producers are not averse to competing on a fair basis in any open farm product market in Japan, but Australia has no desire to grant concessions for easier Japanese entry into the Australian market in exchange for improved access to the Japanese market, only to have these gains eliminated by the dumping of surpluses by an enlarged EEC for example. Those sentiments apply equally well to the United States, Canada and New Zealand, the first two of which have already felt the damaging effects of EEC tactics in disposing of large quantities of surplus barley on the Japanese market in 1969. Any agreement involving Japan and Australia would have to include clear understandings on this issue.

Beyond agriculture, Australia also has an interest in access to Japanese markets for semi-processed and processed non-agricultural commodities. In this regard, clearer specification of Japanese policies towards investment links and import competition in the intermediate goods industries is required.

Since Pacific exporters of temperate zone agricultural products share Australia's interest in the Japanese market, the possibilities for broader negotiations in such a situation are not likely to be lost on Japan. Although Australia is an important market for Japanese exports, any gains Japan may make in terms of improved access to the Australian market alone will probably not be sufficient for her to dismantle or significantly lower her barriers on agricultural trade to advantage of third countries in the Pacific area. It is in Japan's interests to engage all Pacific exporters of farm products in negotiations for increased access to her market. Similarly, it is in Australia's (and others') interests to engage Japan in negotiations over agricultural trade not only to increase direct access to that market, but also in an attempt to prevent closer Japanese links with the EEC without adequate safeguards on agricultural trade.

4.3 Trade Liberalization – Bilateral and Regional

The interests of all Pacific farm product exporters in the growing Japanese market and the relationships between these countries and the less developed areas in the region, together with their mutual interests in factors affecting world trade more generally, suggest the need for a broader arena for trade negotiations. Japan could offer greater liberalisation of her import barriers to agricultural trade, the more widely concessions could be won for her exports. This suggests the interesting possibility of some negotiation which is multilateral in character although confined to Japan and the prinpal exporters of temperate zone agricultural products.[60] There are of course other reasons for looking for the exploitation of a more effective regional framework than any now available.[61]

[60] Any concessions made would be open to GATT partners and it might be expected that Argentina might seek to be associated.

[61] See Peter Drysdale, 'Pacific Economic Integration, An Australian View'; Kiyoshi Kojima, 'Japan's Interest in The Pacific Trade Expansion', in Kiyoshi Kojima, ed., *Pacific Trade and Development*, Japan Economic Research Centre, February, 1968; H. W. Arndt, 'PAFTA: An Australian Assessment', and a reply by Kiyoshi Kojima, 'A Pacific Free Trade Area: Reconsidered', in H. W. Arndt, *A small Rich Industrial Country; Studies in Australian Development, Aid, and Trade*, Melbourne, 1968; Brian Fernon, *Issues in World Farm Trade: Chaos or Co-operation, op. cit.*

Accordingly, while Australia and Japan should continue to exploit their bilateral relations in the direction of further trade investment and economic co-operation, the regional possibilities should be further explored. The importance of the Japanese market to other Pacific countries; the need for Japan to secure growing export markets and import supplies; and the concern of all countries with political stability in the Asian-Pacific area, all point to the importance of greater regional co-operation, not only in trade matters but also in investment, tourism, economic stabilisation policies, and development aid.

One idea that has been floated in recent years is that Japan, Australia, New Zealand and possibly North America might establish a free trade area and offer associate membership to interested less developed countries. This proposal establishes a useful focus but is premature.[62] Moreover, the opportunities for pushing trade liberalisation on a most favoured nation basis are still promising and would be less damaging to global trading arrangements.

The lack of enthusiasm for a free trade area in the Pacific should not, however, be allowed to cloud the prospects for a further substantial freeing of trade and greater economic co-operation within the region. Already there is a disparate collection of joint endeavours at a business-to-business and government-to-government level within the region. Although there are undoubtedly close relations between the Japanese delegations and their Government, the same is far less apparent in respect to other delegations. In any case their meetings are no substitute for inter-governmental relations. Recently a Japan-Australia Joint Consultative Committee has been established. This is to be welcomed. There have long been regular consultations on economic and other matters between the Japanese and American governments.

The interests of all Pacific countries would be better served by a more effectively co-ordinated approach to regional trade and economic problems. The suggestion that bilateral government-to-government consultations and negotiations within the framework of an Organisation for Pacific Trade Aid and Development would appear sound. OPTAD could be developed along similar lines to OECD, that is, not as a regulatory agency but as a place where government-to-government consultations could take place. Although this is already a function of OECD, Japan, Australia, the United States and Canada, the four leading nations of the Pacific area, are the only non-European nations out of a total OECD membership of 23 and thus there would appear to be considerable advantages in having a smaller scale regional organisation to deal with problems of a more regional nature that may well be frustrated in OECD, or even in GATT, in which European interests tend to frustrate world-wide progress.

OPTAD should in no way be thought of as some sort of a substitute for OECD or GATT but a complementary organisation to facilitate the discussion and speed the resolution of regional problems. Such an organisation would also play a useful role in broadening the area of trade negotiations and lessening the danger that important bilateral talks such as those between

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[62] See J. G. Crawford, Introduction to, Brian Fernon, *op. cit.*; Kiyoshi Kojima, 'A Pacific Free Trade Area: A New Design For World Trade Expansion', *Hitotsubashi Journal of Economics*, Vol. 12, No. 1, June, 1971.

Japan and the United States over textiles, for example, could be held with such scant regard for the welfare of the other affected parties.[63]

In addition, OPTAD could act as a stimulant to joint aid and investment programs in the region and, in general provide a framework within which negotiations and discussions for furthering the economic development of the Asian area could take place.

Further, OPTAD could provide a more secure framework of economic alliance from within which participant countries could play a less suspect and more useful role of conciliation toward China.

In terms of further liberalisation of trade, the importance of the Japanese market to the major Pacific exporters is such that it is in Japan's interests to engage all the farm product exporters of the Pacific area, in a bargaining round. At present this could only be done via a series of bilateral exchanges between interested parties. Only then would Japan be likely to gain sufficient benefits to compensate her for the significant liberalisation that she is being called on to give all four Pacific exporters.

This partial collective approach to the problems of Japanese access to the developed markets in the Pacific and access to Japanese markets by the agricultural exporters is to be preferred by Australia, New Zealand and Canada to a situation in which they and the world must await the dubious results of a major bilateral trade war between the United States and Japan. Such a trade war could really produce difficult questions for Australia if the United States became very restrictionist towards Japan. Japan might then offer Australia concessions which would be denied to the United States, GATT or no GATT. Australia might, for the sake of her agriculture, have to choose Japan and risk retaliation from the United States. The prospect is not inviting and may serve as a spur towards greater regional efforts to resolve the present difficulties between the two leading trading partners in the Pacific.

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[63] These comments are substantially in agreement with those of Professor Kojima, the original publicist of the Pacific Free Trade Area approach, who has indicated recently that OPTAD does offer scope for a more practical approach to problems of economic co-operation in the Pacific area. See Kiyoshi Kojima, 'A Pacific Free Trade Area: A New Design For World Trade Expansion', *op. cit.*

APPENDIX 1

Gross Value of Farm Production, Farm Cost, Farm Income, and Index of Volume of Farm Output; Australia; 1960-61 to 1970-71

Year	Index of Volume of Farm Output[a]	Gross Value of Farm Production[b]	Farm Costs[c]	Farm Income[d]
		$Am	$Am	$Am
1960-61	152	2,745	1,728	1,017
1961-62	155	2,734	1,792	942
1962-63	166	3,013	1,875	1,138
1963-64	174	3,425	1,994	1,431
1964-65	181	3,451	2,137	1,314
1965-66	166	3,347	2,286	1,061
1966-67	198	3,828	2,456	1,372
1967-68	175	3,345	2,524	821
1968-69	215	3,956	2,711	1,245
1969-70	207	3,773	2,741	1,032
1970-71[e]	198	3,631	2,740	891

[a] Base: average 1936-37 to 1938-39 = 100.

[b] Production of the various commodities is valued at the wholesale prices realised in the principal markets and includes subsidies, etc.

[c] Total costs are cash costs such as wages, rent, interest, marketing costs, etc., and depreciation.

[d] Gross value of farm production less total farm costs.

[e] Estimated by the Bureau of Agricultural Economics.

Source: *Trends in Australia's Rural Production and Exports*, Bureau of Agricultural Economics, Canberra (various issues).

APPENDIX 2

Indexes of Prices Paid by Australian Farmers and Prices Received on Domestic and Export Markets

Base: Average 1960-61 to 1962-63 = 100

Year	Prices Paid	Prices Received			Ratio of Prices Received to Prices Paid
		Domestic	Export	All Markets	
1960-61	99	107	97	103	104
1961-62	100	95	99	97	97
1962-63	101	98	104	101	100
1963-64	101	101	121	109	108
1964-65	105	107	104	106	101
1965-66	111	116	107	111	100
1966-67	114	117	105	110	96
1967-68	118	119	95	107	91
1968-69	120	117	98	106	88
1969-70	121	118	92	101	83
1970-71[a]	126	119	83	98	78

[a] Estimated by Bureau of Agricultural Economics.

Source: Bureau of Agricultural Economics, Canberra.

APPENDIX 3

Levies in the EEC Expressed as a Proportion of World Prices for Selected Commodities 1968-69[a]

Commodities	Percentage
Grains[b]	
Soft wheat	82
Hard wheat	63
Rye	78
Barley	98
Oats	81
Maize	74
Sugar	
Raw Sugar	230
Dairy Products[c]	
Butter	403
Cattle[d]	
Calves and young fattening stock	18
Fat cattle	59
Slaughter cows	37

[a] Measures an arithmetic average of monthly levies charged during 1968-69 as a proportion of actual average c.i.f. import prices for the year.

[b] For grains the import prices used are the arithmetic averages of the most commonly imported grades.

[c] Average c.i.f. price of imports from all non-members.

[d] For cattle the levies include calculated *ad valorem* tariffs.

Figures obtained from Directeur Général de l'Agriculture, *Marchés Agricoles Prix*, Brussels (various issues); OECD, *Trade by Commodities: Market Summaries: Imports*, Paris (various issues).

Source: A. C. Byrne, 'The Common Agricultural Policy of the EEC', *Quarterly Review of Agricultural Economics*, Vol. XXIV, No. 2, April 1971, p. 87.

APPENDIX 4

Value of Australian Agricultural Exports by Major Destinations[a c]

Year	United Kingdom		Japan		E.E.C.		North America		Communist Countries		Other		Total Agricultural Exports		Agricultural Exports as % of Total Exports
	$Am	%	$Am	%	$Am	%	$Am	%	$Am	%	$Am	%	$Am	%	
1955-56	453	35.9	166	13.2	326	25.9	87	6.9	35	2.8	192	15.3	1259	100.0	82.5
1956-57	492	31.3	239	15.2	446	28.4	86	5.5	56	3.6	252	16.0	1571	100.0	81.1
1957-58	389	30.7	185	14.6	346	27.3	81	6.4	73	5.8	193	15.2	1267	100.0	79.0
1958-59	457	35.9	183	14.4	256	20.1	126	9.9	54	4.3	199	15.4	1275	100.0	79.7
1959-60	417	28.4	227	15.5	333	22.7	142	9.7	104	7.1	247	16.6	1470	100.0	79.9
1960-61	341	24.1	249	17.7	298	21.1	125	8.9	140	9.9	259	18.3	1412	100.0	78.0
1961-62	353	21.4	276	16.8	335	20.4	188	11.4	185	11.2	308	18.8	1645	100.0	78.9
1962-63	333	20.1	278	16.8	299	18.0	258	15.6	184	11.1	305	18.4	1657	100.0	79.2
1963-64	421	19.5	395	18.3	390	18.0	276	12.8	319	14.7	363	16.7	2164	100.0	79.8
1964-65	412	21.2	338	17.4	336	17.3	232	12.0	244	12.6	378	19.5	1940	100.0	76.0
1965-66	359	19.3	341	18.3	353	19.0	277	14.9	186	10.0	346	18.5	1862	100.0	67.1
1966-67	311	15.4	389	19.2	346	17.1	291	14.4	186	9.2	499	24.7	2022	100.0	65.7
1967-68	275	15.0	359	19.6	294	16.0	301	16.4	185	10.1	425	22.9	1839	100.0	59.3
1968-69	265	14.1	416	22.1	342	18.2	341	18.2	140	7.5	374	19.9	1878	100.0	54.7
1969-70	306	14.5	434	20.5	336	15.9	411	19.4	206	9.7	423	20.0	2116	100.0	50.4
1970-71[b]	317	14.7	424	19.7	245	11.4	368	17.1	178	8.3	619	28.8	2151	100.0	49.1

[a] Includes re-exports.

[b] Preliminary.

[c] Agricultural exports include the following SITC groups: 00 Live Animals; 01 Meat and Meat Preparations; 02 Dairy Products and Eggs; 04 Cereals and Cereal Preparations; 05 Fruit and Vegetables; 06 Sugar and Sugar Preparations; 07 Coffee, Cocoa, Tea, etc.; 08 Animal Feedstuffs; 09 Miscellaneous Foodstuffs; 11 Beverages (ex. distilled alcoholic); 121 Unmanufactured Tobacco; 21 Hides and Skins; 22 Oilseeds, Nuts and Kernels; 231.1 Natural Rubber; 261-265 Natural Fibres; 29 Crude Animal and Vegetable Materials; 4 Animal and Vegetable Oils and Fats; 555.1, 599.5, Esttential Oils, Casein, Albumen, etc.

Source: *Overseas Trade*, Commonwealth Bureau of Census and Statistics, Canberra (various issues).

APPENDIX 5

Pacific Country Exports to Japan, EEC, and United Kingdom:
Major Commodities: Selected Years

	Total Exports $USm	Percentage of Total to: Japan	EEC	United Kingdom	Total Exports $USm	Percentage of Total to: Japan	EEC	United Kingdom
		Beef and Veal				Mutton and Lamb		
United States								
1962	6.7	—	—	1.5	0.8	—	—	—
1965	18.9	—	7.9	2.1	—	—	—	—
1969	17.8	3.3	1.7	1.1	1.0	—	—	—
Canada								
1962	7.7	—	—	—	0.3	—	—	—
1965	27.5	—	6.5	—	—	—	—	—
1969	29.1	—	—	—	2.1	—	—	—
Australia								
1962	a				a			
1965	212.0	2.0	8.4	29.7	43.5	20.0	1.1	20.9
1969	283.9	3.7	0.1	4.4	70.7	19.5	0.4	17.7
New Zealand								
1962	a				a			
1965	72.9	2.1	10.7	22.5	175.8	5.4	1.2	86.7
1969	152.1	1.6	0.3	8.3	215.7	11.0	1.3	79.6
		Pork				Animal Oils and Fats		
United States								
1962	10.2	—	—	—	111.6	14.5	32.4	2.6
1965	8.2	—	—	—	193.1	18.0	21.1	4.5
1969	51.8	51.9	—	—	131.6	22.6	10.0	2.8

(Cont'd on p. 46)

APPENDIX 5 *(cont'd)*

	Total Exports $USm	Percentage of Total to: Japan	EEC	United Kingdom	Total Exports $USm	Percentage of Total to: Japan	EEC	United Kingdom
Canada								
1962	13.7	—	—	—	6.4	15.6	14.1	15.6
1965	18.6	—	—	—	13.5	14.8	14.0	35.6
1969	24.9	11.2	—	—	9.7	34.0	16.5	27.8
Australia								
1962	[a]				16.0	10.0	5.6	20.0
1965	0.5	—	—	—	18.2	4.9	5.5	16.5
1969	4.6	86.9	—	—	20.8	28.3	18.3	2.9
New Zealand								
1962	[a]				7.8	6.4	—	26.9
1965	2.1	—	23.8	23.8	10.3	8.7	5.8	27.2
1969	0.7	14.3	42.9	—	9.1	20.9	20.9	13.2
	Milk and Cream Dry				Butter			
United States								
1962	82.6	9.4	5.1	—	2.0	—	25.0	—
1965	125.9	8.0	15.3	—	29.7	2.7	36.0	—
1969	76.3	2.2	0.7	—	14.6	—	—	—
Canada								
1962	11.0	—	3.6	—	—	—	—	—
1965	22.1	—	26.2	1.0	4.3	—	62.7	20.9
1969	17.0	3.5	10.6	—	—	—	—	—
Australia								
1962	[a]				50.1	0.4	2.6	78.4
1965	12.1	2.5	—	10.7	67.2	0.9	1.2	66.2
1969	19.5	4.6	—	5.6	46.6	0.1	—	49.7

New Zealand								
1962	[a]				122.7	0.2	0.4	91.0
1965	28.6	3.8	1.7	43.0	157.9	0.3	0.3	87.1
1969	28.5	16.1	—	17.5	135.0	0.1	0.2	91.8
		Cheese and Curd				Casein, Gluten, etc.		
United States								
1962	6.3	—	—	4.7	13.7	3.7	12.4	7.3
1965	3.5	—	—	—	23.4	20.5	15.0	14.1
1969	4.4	11.4	—	—	27.1	3.7	12.9	15.1
Canada								
1962	8.3	—	—	94.0	4.6	—	—	15.2
1965	10.8	—	—	94.4	8.5	—	—	15.3
1969	13.3	—	—	65.4	7.5	—	2.7	2.7
Australia								
1962	11.8	5.9	3.4	53.4	9.9	13.1	4.0	13.1
1965	15.8	10.1	6.7	40.5	12.2	32.0	3.3	14.8
1969	18.7	23.0	—	28.9	19.2	25.0	7.8	18.2
New Zealand								
1962	52.6	1.0	0.8	87.8	11.4	27.2	23.7	26.3
1965	53.9	1.3	4.3	82.9	24.7	15.4	34.4	16.2
1969	50.8	5.5	1.0	77.0	28.5	22.1	31.9	9.8
		Wheat Unmilled				Maize Unmilled		
United States								
1962	941.3	5.8	5.4	2.0	529.2	9.6	31.6	23.5
1965	1,063.6	10.3	6.4	1.7	832.7	16.5	41.0	11.0
1969	725.9	16.4	7.7	0.4	726.0	26.3	30.4	9.8
Canada								
1962	561.6	14.5	21.6	23.3	—	—	—	—
1965	777.2	10.7	14.9	16.7	1.9	—	36.8	42.1
1969	437.3	16.1	20.6	18.6	1.0	—	—	—

(Cont'd on p. 48)

	Total Exports $USm	Percentage of Total to: Japan	EEC	United Kingdom	Total Exports $USm	Percentage of Total to: Japan	EEC	United Kingdom
Australia								
1962	245.9	10.8	8.0	12.6	—	—	—	—
1965	377.2	6.4	0.1	9.3	—	—	—	—
1969	360.4	20.7	5.0	16.3	—	—	—	—
New Zealand								
1962	—	—	—	—	—	—	—	—
1965	—	—	—	—	—	—	—	—
1969	2.7	—	—	—	—	—	—	—
	Cereals Unmilled, n.e.s.				Animal Feeding Stuffs			
United States								
1962	122.1	18.1	51.8	8.8	140.6	5.8	44.0	1.0
1965	229.7	30.7	45.0	3.7	277.7	10.1	49.9	2.9
1969	138.7	63.8	4.7	0.1	405.5	8.6	58.5	1.1
Canada								
1962	16.2	1.9	51.2	11.1	40.6	6.4	—	52.2
1965	23.6	8.9	52.5	5.1	61.7	7.3	0.3	49.3
1969	8.5	29.4	7.1	9.4	57.5	8.3	0.5	34.6
Australia								
1962	17.4	2.3	40.8	24.7	8.6	10.5	4.7	10.5
1965	15.2	4.6	57.2	4.6	5.7	22.8	—	—
1969	16.1	26.7	48.4	14.3	12.7	28.3	—	3.2
New Zealand								
1962	—	—	—	—	1.2	16.7	16.7	25.0
1965	—	—	—	—	2.0	55.0	9.1	20.0
1969	—	—	—	—	4.7	51.1	—	6.4

	Fruit and Vegetables				Oilseeds, Nuts and Kernels			
United States								
1962	443.4	2.1	20.9	11.5	428.5	26.1	40.6	3.3
1965	487.0	3.7	21.6	8.5	706.8	24.2	34.6	3.6
1969	539.3	7.0	17.3	6.2	871.8	23.6	34.0	2.0
Canada								
1962	40.2	—	6.2	36.6	68.4	23.0	35.2	33.3
1965	58.8	—	7.0	32.5	90.9	27.5	30.7	27.4
1969	74.5	0.5	4.3	31.1	87.4	45.5	29.3	9.8
Australia								
1962	94.0	0.6	7.4	63.7	—	—	—	—
1965	110.6	0.5	14.6	51.3	0.3	—	—	—
1969	95.8	1.0	10.0	43.3	1.6	50.0	12.5	18.8
New Zealand								
1962	12.0	—	15.8	60.0	—	—	—	—
1965	14.4	—	9.7	50.7	—	—	—	—
1969	21.3	4.2	13.6	38.0	—	—	—	—

	Hides and Skins				Wool			
United States								
1962	82.9	38.4	24.8	2.3	—	—	—	—
1965	109.4	26.6	29.3	4.6	—	—	—	—
1969	152.4	36.1	16.2	3.5	—	—	—	—
Canada								
1962	14.0	16.4	35.7	5.7	2.3	—	—	13.0
1965	21.1	13.3	35.5	6.6	2.4	—	—	—
1969	54.8	8.4	19.5	17.9	1.0	—	—	—
Australia								
1962	75.1	12.7	68.6	5.7	831.9	28.8	29.7	14.6
1965	85.8	4.8	72.0	10.4	846.4	32.3	28.9	11.8
1969	96.8	12.9	69.9	3.1	866.8	34.9	29.0	8.7

(Cont'd on p.50)

APPENDIX 5 *(cont'd)*

	Total Exports $USm	Percentage of Total to: Japan	EEC	United Kingdom	Total Exports $USm	Percentage of Total to: Japan	EEC	United Kingdom
New Zealand								
1962	34.4	3.8	36.6	11.0	269.7	4.3	42.6	28.3
1965	43.5	1.0	29.9	13.3	284.7	8.4	37.6	21.6
1969	62.4	4.0	41.0	18.3	246.2	10.9	36.7	20.2

[a] Data unavailable.

Source: United Nations, *Commodity Trade Statistics* (various issues).

APPENDIX 6

Australian Agricultural Exports 'At Risk' on U.K. Entry to EEC 1970-71[p]

Commodity	Total Exports	Exports to UK	Value of Total Production[b]	Exports to UK as % of Total Exports	Exports to UK as % Total Production	Market Regulations Under the Common Agricultural Policy of EEC	Trade Barriers in Japanese Market
	$Am	$Am	$Am	%	%		
Wheat[a]	434.0	81.5	408.0	18.8	20.0	Variable import levies, and export subsidies.	State trading.
Beef and veal	304.9	21.0	634.0	6.9	3.3	*Ad valorem* tariff 20%, plus variable import levies and export subsidies.	Import quotas, tariff 25%, plus additional levy.
Mutton and lamb	74.2	14.4	170.0	19.4	8.5	Not under CAP yet. Common External Tariff 20%, quantitative restrictions by individual EEC members.	Tariff, 7.5%.
Butter	48.2	29.1	180.0	60.4	16.2	Variable import levies and export subsidies.	State trading.
Cheese	18.9	4.2	34.0	22.2	12.4	Variable import levies and export subsidies.	Processed cheese quantitatively restricted; tariff 35% reducing to 10% on natural cheese.

(Cont'd on p. 52)

APPENDIX 6 *(cont'd)*

Commodity	Total Exports	Exports to UK	Value of Total Production[b]	Exports to UK as % of Total Exports	Exports to UK as % Total Production	Market Regulations Under the Common Agricultural Policy of EEC	Trade Barriers in Japanese Market
Sugar (raw)	149.7	40.4	157.0	27.0	25.7	Variable import levies and export subsidies.	Minimum import price, tariff of $104 per ton, plus consumption tax $48 per ton refined sugar.
Canned fruit	42.9	27.7	n.a.	64.6	n.a.	Not under CAP yet, CET of 24%, plus levy on sugar content, and quantitative restrictions by individual members.	Some quantitative restrictions and tariffs up to 55%.
Dried vine fruits	18.5	7.1	21.0	38.4	33.8	Tariff quotas, quota restrictions. Preferences to Greece, Turkey, Spain.	*Ad valorem* tariff, 20%.
Fresh apples	21.9	10.3	57.0	47.0	18.1	Tariff, seasonal quotas and supplementary levies.	Strict quarantine provisions prevent exports from Australia.
Fresh pears	6.4	1.4	21.9	21.9	6.4		

[a] Value of exports greater than value of production due to sales from stocks.

[b] Estimated by Bureau of Agricultural Economics; see *Trends in Australia's Rural Production and Exports*, June 1971.

[p] Preliminary.

APPENDIX 7

Composition of Australia's Agricultural Exports

	1955-56		1960-61		1964-65		1969-70		1970-71[a]	
	$Am	%	$Am	%	$Am	%	$Am	%	$Am	%
Meats	120.9	9.6	144.8	10.3	286.4	14.8	420.6	19.9	430.8	20.0
Dairy products and eggs	97.2	7.7	79.1	5.6	113.1	5.8	102.3	4.8	102.2	4.8
Cereals	173.4	13.8	301.8	21.4	394.1	20.3	433.9	20.5	597.2	27.8
Fruit and vegetables	69.0	5.5	61.4	4.3	86.0	4.4	94.8	4.5	107.1	5.0
Sugar and honey	52.6	4.2	71.6	5.1	114.1	5.9	121.8	5.8	160.1	7.4
Hides and skins	41.8	3.3	54.4	3.9	80.1	4.1	90.0	4.3	71.8	3.3
Wool	675.1	53.6	669.6	47.4	806.1	41.5	762.0	36.0	544.4	25.3
Other	29.5	2.3	29.0	2.0	60.4	3.2	90.3	4.2	137.8	6.4
Total	1,259.5	100.0	1,411.7	100.0	1,940.3	100.0	2,115.7	100.0	2,151.4	100.0

[a] Preliminary.

Source: *Overseas Trade*, Bureau of Census and Statistics, Canberra (various issues).

APPENDIX 8

Japanese Agricultural Production
(Calendar years)

Product	Units	1960	1963	1965	1966	1967	1968	1969	1970
Rice	'000 tons	12,858	12,810	12,409	12,745	14,453	14,449	14,003	12,689
Wheat	"	1,531	716	1,287	1,024	997	1,012	758	474
Barley	"	2,301	759	1,234	1,105	1,032	1,021	812	573
Sweet potatoes	"	6,277	6,662	4,955	4,810	4,031	3,594	2,855	2,564
Potatoes	"	3,594	3,409	4,056	3,383	3,638	4,056	3,575	n.a.
Oranges	"	1,072	1,113	1,568	2,000	1,850	2,589	2,392	n.a.
Beef	"	142	186	208	155	158	176	237	n.a.
Pig meat	"	147	279	364	565	603	590	588	n.a.
Milk	"	1,887	2,761	3,221	3,409	3,566	4,014	4,513	n.a.
Butter	"	12	22	24	25	24	32	42	n.a.
Cheese	"	5	12	16	27	31	33	38	n.a.
Eggs	Millions	9,560	15,300	18,625	18,756	23,307	24,694	27,898	n.a.
Cattle	'000	3,164	3,482	3,175	2,887	2,928	3,155	3,458	3,593
Pigs	"	1,918	3,296	3,976	5,158	5,975	5,535	5,429	6,335
Chickens	"	54,627	98,447	138,476	136,420	157,408	165,820	198,377	223,531

Source: Ministry of Agriculture and Forestry, *Statistical Report*, Tokyo, Japan (various issues).

APPENDIX 9

Japan's Imports of Major Agricultural Commodities by Principal Source: Selected Years[a]

	1964 $USm	1966 $USm	1969 $USm	1970 $USm
Wheat	262.0	278.8	297.0	318.4
US	120.1	149.4	133.0	173.7
Canada	106.4	104.1	75.8	87.2
Australia	33.7	25.3	83.2	57.5
Barley	29.3	30.7	34.4	41.6
Canada	5.0	9.3	2.6	30.0
Australia	7.4	3.1	9.0	6.3
EEC	—	—	22.2	5.4
US	16.8	18.4	0.5	—
Maize	208.7	243.3	331.9	406.9
US	101.3	153.2	207.2	292.8
Thailand	45.2	50.2	26.5	37.0
South Africa	41.5	—	41.2	27.9
Argentina	0.7	1.2	10.8	29.0
Australia	—	—	—	1.3
Sorghum	61.2	133.1	161.5	235.2
US	48.0	117.7	108.5	134.5
Argentina	12.9	10.7	47.6	78.9
Australia	0.2	0.9	0.2	16.7
Beef and Veal	3.7	10.6	15.8	22.3
Australia	3.1	7.1	12.2	18.1
New Zealand	0.4	2.2	2.6	2.5
US	—	—	0.4	1.4
Mutton and Lamb	22.7	39.0	47.0	49.9
New Zealand	13.4	21.1	31.1	28.5
Australia	9.2	17.9	15.9	21.3
Pork	3.1	—	51.7	20.9
US	2.9	—	35.0	8.9
Taiwan	—	—	7.8	5.1
Canada	—	—	3.2	4.6
Australia	—	—	4.4	0.8
Butter	0.1	6.5	0.2	0.7
Australia	0.1	2.4	0.2	0.5
New Zealand	—	3.2	—	0.1
EEC	—	0.5	—	0.1

(Cont'd on p. 56)

APPENDIX 9 *(cont'd)*

	1964 $USm	1966 $USm	1969 $USm	1970 $USm
Cheese	5.2	12.4	17.3	20.0
Australia	1.4	3.8	5.2	6.0
New Zealand	1.0	2.0	3.3	3.6
Norway	1.2	2.8	4.1	4.2
EEC	1.3	2.4	2.6	3.4
Denmark	0.2	0.6	1.2	1.3
Skim Milk Powder (School Lunch Program)	13.0	12.5	5.6	2.8
New Zealand	0.7	3.5	3.0	2.4
US	12.3	6.4	0.8	0.4
EEC	—	—	1.8	—
Skim Milk Powder (Feed)	0.7	3.4	5.1	8.3
EEC	—	2.4	1.6	4.6
New Zealand	—	0.7	2.5	2.3
Australia	—	0.1	0.4	0.5
Canada	—	—	0.5	0.6
Eggs	0.1	1.4	10.2	14.0
Australia	—	1.0	4.1	6.3
UK	—	0.1	2.9	2.2
South Africa	—	—	1.5	1.4
Bananas	55.2	65.1	116.5	144.1
Ecuador	22.3	10.7	41.9	80.9
Taiwan	32.3	53.4	56.9	36.3
Honduras	—	—	12.4	1.2
Lemons	5.4	9.0	19.7	24.1
US	5.4	9.0	19.7	24.1
Dried Vine Fruit	7.4	6.7	7.2	7.3
US	6.3	5.5	6.5	6.8
Australia	0.6	0.4	0.4	0.2
Greasy Wool	365.5	402.9	369.7	322.8
Australia	311.1	317.3	312.4	274.3
New Zealand	19.5	39.8	16.7	13.0
South Africa	21.0	26.2	26.8	23.7
Cotton	432.0	413.9	414.2	461.4
Mexico	113.5	115.3	106.8	77.0
US	141.5	110.3	59.0	76.7

(Cont'd on p. 57)

APPENDIX 9 *(cont'd)*

	1964 $USm	1966 $USm	1969 $USm	1970 $USm
Brazil	13.1	13.3	37.1	43.3
Nicaragua	23.6	36.6	31.4	25.8
UAR	17.2	13.6	27.1	25.6
India	20.3	14.3	17.2	19.3
Pakistan	14.2	13.0	7.6	9.1
Australia	—	—	2.5	2.6
Sugar (raw)	241.6	123.6	196.9	280.1
Cuba	53.3	20.0	64.0	106.3
Ryukyu	33.6	42.3	46.7	45.8
Australia	51.3	30.1	41.3	51.6
South Africa	29.1	8.8	25.0	37.1
Taiwan	61.1	19.3	9.9	10.3
Soybeans	184.5	272.0	281.0	365.8
US	153.9	222.3	238.7	329.6
China	30.5	49.2	42.3	36.0
Rapeseed	9.2	25.0	28.1	41.4
Canada	9.0	21.5	25.2	39.6
China	—	3.5	0.2	—
Linseed	12.5	14.4	16.9	17.3
Canada	12.3	14.4	16.5	16.9
Australia	—	—	0.4	0.3
Hides and Skins	48.6	91.5	96.7	93.0
US	32.1	54.8	61.7	64.3
Australia	7.2	15.3	13.4	10.9
EEC	n.a.	3.1	5.1	4.3
Canada	1.9	6.5	4.2	3.1
New Zealand	0.7	2.0	2.8	3.0

[a] Calendar years, c.i.f.

Source: Ministry of Finance, *Japan Exports and Imports*, Tokyo (various issues).

APPENDIX 10

Per Capita Consumption of Selected Food Products: Japan
(Kilograms per year)

	Average 1955-59	1962	1965	1968	1969
Rice	113.7	118.3	111.7	100.1	96.9
Wheat	25.1	26.0	29.0	31.3	31.3
Barley	12.7	2.5	3.6	2.9	2.2
Potatoes	40.5	27.7	22.8	18.3	16.9
Meat	4.4	7.9	9.0	11.0	12.2
Eggs	4.0	6.9	8.8	11.7	12.6
Dairy Products	18.8	28.4	37.4	44.8	47.3
Sugar	13.7	17.0	18.8	22.2	24.2
Vegetables	83.4	102.6	109.6	124.9	120.1
Fruits	21.7	23.4	28.5	38.2	36.6
Fish and Products	24.3	29.9	29.2	32.3	30.7
Fats and Oils	3.5	5.3	6.8	8.5	9.1
Average Daily Calorie Intake	2253	2373	2417	2460	2447

Source: Ministry of Agriculture and Forestry, *Food Balance Sheets 1955-1969*, Japan.

APPENDIX 11

Daily per Capita Calorie and Protein Intake: Selected Countries

	Calories	Total Protein	Animal Protein
		grams	grams
New Zealand	3290	107.3	74.3
US	3240	96.1	69.6
France	3180	99.8	60.3
Canada	3180	95.4	64.1
UK	3180	88.0	54.0
USSR	3150	91.5	35.8
Hungary	3140	97.0	41.3
Poland	3110	93.2	42.6
Australia	3110	91.6	62.0
West Germany	2960	80.5	51.6
United Arab Republic	2960	76.3	10.7
Italy	2940	87.2	37.8
Greece	2900	98.9	43.0
Mexico	2600	66.8	15.1
Japan	2459	75.7	29.5
Pakistan	2230	50.6	10.1
Philippines	2010	51.9	19.9

Source: FAO, *The State of Food and Agriculture 1970*, Rome, 1970.
Data is for 1968 except for USSR and Poland which are average figures 1964-66.

APPENDIX 12

Consumer Price Index: Composition and Rate of Increase, 1965-1969

	1965-69 (Annual Rate)	
	Rate of Increase, %	% Contribution
General	4.9	100
Commodities	4.5	63
Foods	5.2	42
Liberalised items	4.6	17
Items under Import Restriction	4.9	13
Governmental trade items	7.1	12
Other Commodities	3.6	21
Liberalised items	3.5	19
Items under Import Restriction	3.7	1
Governmental trade items	4.4	1
Services	5.8	37

Source: Economic Planning Agency, *Economic Survey of Japan, 1969-70*, Tokyo, p. 142.

APPENDIX 13

Ratio of Domestic Production to Consumption: Japan
(per cent)

	1963	1969	1977 Projection
Rice	99.3	117.0	100.0
Wheat	38.2	14.5	13.7
Barley	87.3	47.5	44.5
Soybeans	21.0	4.7	2.9
Vegetables	100.1	99.4	100.5
Fruits	100.6	84.7	86.5
Dairy Products	82.2	91.4	91.4
Meats (ex whale)	94.6	82.9	88.3
Eggs	100.8	98.0	98.5
Sugar and products	45.6	45.0	n.a.
Fish and shell fish	108.0	100.4	n.a.
Other cereals (mainly feed)	11.9	1.7	n.a.

Source: Ministry of Agriculture and Forestry, *Food Balance Sheets (1963, 1969); Long Term Projection of Supply and Demand for Agricultural Products*, Tokyo, 1968 (in Japanese)

APPENDIX 14

Exports of Agricultural Products[1] of United States, Canada and New Zealand, 1965 and 1969[3]

($US millions)

Agricultural Exports f.o.b. to	United States		Canada		New Zealand	
	1965[2]	1969[2]	1965	1969	1965	1969
United States	—	—	271.8	297.2	117.2	171.7
Canada	629.3	722.5	—	—	10.2	37.5
Latin America	436.3	447.9	79.0	63.0	6.7	6.4
EEC	1,475.0	1,302.2	201.5	142.0	150.5	144.2
United Kingdom	407.6	376.2	310.9	238.8	468.5	461.2
Australia	40.3	36.6	2.1	4.1	10.8	16.3
New Zealand	6.7	6.6	0.3	0.4	—	—
Pacific Islands	4.8	7.7	—	—	7.2	10.6
Japan	884.5	936.9	132.7	136.5	44.3	78.5
'Other Asia'	1,056.2	1,101.5	40.2	55.0	31.8	33.1
Middle East	306.0	183.1	21.0	8.6	3.3	3.1
Communist countries	101.5	88.1	360.7	119.0	12.5	23.5
Other destinations	948.8	819.5	84.8	87.1	59.1	45.6
Total Agricultural Exports	6,297	6,029	1,495	1,151	922	1,032
Total Exports	27,003	37,444	8,107	13,754	979	1,182
Total Exports to Japan	2,042	3,462	293	579	50	108
Percentage Agricultural of Total Exports	23	16	18	8	94	87
Percentage Agricultural Exports to Japan of Total Exports to Japan	43	27	45	24	89	73

[1] Includes processed oils and fats.

[2] Includes re-exports valued at $US80 millions in both 1965 and 1969. In 1969 Canada received $US51m; Latin America $US5m; EEC $US7m; UK $US5m; 'Other Asia' $US6m; Japan $US0.7m in re-exports.

[3] In 1969 United States exports were affected by a longshoremen's strike. Total exports in 1970 were $US42,028m and agricultural exports $US7,174m. Exports to both EEC and Japan were a record. The increase in exports to EEC to $US1,559m was mainly due to an increase of $US155m sales of oilseeds (not subject to variable levy).

Source: Compiled from UN *Commodity Trade Statistics* 1965, and 1969.

APPENDIX 15

Main Agricultural Exports to Japan 1969

$US millions

United States		Canada		New Zealand	
Soyabeans (221.4)	200.3	Wheat (041)	70.5	Wool (262.1,.2)	26.9
Corn (044)	190.6	Rapeseed, mustardseed[1] etc. (221.8)	23.8	Mutton and lamb (011.2)	23.7
Wheat (041)	119.3			Casein[1], etc. (599.5)	6.3
Sorghum[1], etc. (045.9)	88.4	Linseed (221.5)	16.0	Dried milk (022.2)	4.6
Raw cotton (263.1)	52.1	Animal feeds (081)	4.8	Cheese (024)	2.8
Cow hides, etc. (211.1)	51.0	Hides and skins (211)	4.5	Hides and skins (211)	2.5
Tobacco (121)	44.7	Barley (043)	3.5	Animal feeds (081)	2.4
Inedible tallow[1], etc. (411.3)	29.8	Inedible tallow[1], etc. (411.3)	3.3	Beef and veal (011.1)	2.4
Alfalfa meal[1], etc. (081.9)	29.2	Meat fresh, frozen (011)	3.0	Inedible tallow[1] (411.3)	1.9
Pork (011.3)	26.9	Malt (048.2)	1.8	Lactose and honey (061)	1.2
Lemons, limes (051.2)	11.7	Milk and cream dry (022.2)	1.4	Sausage casings[1], etc. (291)	0.7
Raisins[1], etc. (052)	6.7	Buckwheat[1], etc. (045.9)	1.3	Dried peas and beans[1] (054.2)	0.4

Dried peas and beans (054.2)	6.1	Rye (045.1)	1.1	Peaches in syrup[1] etc. (053.9)	0.1
Preserved peaches[1], etc. etc. (053.9)	5.9				
Essential oils (551.1)	5.5				
Chickens[1], etc. (011.4)	4.7				
Almonds[1], etc. (051.7)	4.6				
Oil cake and meal (081.3)	3.5				
Safflower seeds[1], etc. (292.5)	3.5				
Live chickens[1], etc. (001.4)	3.4				
Lard (091.3)	3.3				
Other agricultural exports	72.7		1.5		2.6
Total Agricultural Exports to Japan	936.9		136.5		78.5

( ) SITC groups or subgroups in brackets.

[1] These are the major items exported to Japan in the group or subgroup.

Source: Compiled from UN *Commodity Trade Statistics 1969*.

APPENDIX 16

Agricultural Exports of United States[1], Canada, New Zealand and Australia to All Destinations, 1969

$US millions	SITC Group or Sub-Group	United States	Canada	New Zealand	Australia
Live animals	00	46.7	47.4	4.2	6.6
Meat and preparations	01	199.4	78.7	399.0	396.6
Beef and veal	011.1	17.8	29.1	152.1	283.9
Lamb and mutton	011.2	1.0	2.1	215.7	70.7
Pork	011.3	51.8	24.9	0.7	4.6
Poultry	011.4	38.5	0.4	—	1.1
Dairy products and eggs	02	130.9	33.9	218.1	96.6
Milk and cream dry	022.2	76.3	17.0	28.5	19.5
Butter	023	14.6	—	135.0	46.6
Cheese	024	4.4	13.3	50.8	18.7
Eggs	025	14.0	2.1	—	7.5
Cereals and preparations	04	2,127.2	552.0	4.6	460.7
Wheat, unmilled	041	725.9	437.3	2.7	360.4
Corn, unmilled	044	726.0	1.0	—	0.1
Other cereals, unmilled	045	138.7	8.5	—	16.1
Fruit and vegetables	05	539.3	74.5	21.3	95.8
Fruit, nuts, fresh	051	195.8	19.6	9.3	32.8
Oranges, etc.	051.1	53.8	—	—	3.6
Lemons, limes, etc.	051.2	39.7	—	—	0.2
Apples	051.4	9.2	13.0	8.0	23.4
Nuts	051.7	34.6	1.2	—	—
Dried fruit	052	50.5	0.2	—	18.6
Fruit, prepared, preserved	053	123.4	8.5	2.6	39.5
Vegetables	054	136.8	33.2	8.4	3.7
Potatoes	054.1	8.1	11.5	0.5	1.4
Dried legumes	054.2	52.9	7.3	4.7	0.6
Sugar and honey	06	22.8	13.5	2.7	134.3
Coffee, tea, spices	07	35.9	15.5	1.4	2.7
Animal feeding stuff	081	405.5	57.5	4.7	12.7
Miscellaneous foods	09	139.1	5.5	1.4	3.5
Margarine, shortening	091	41.9	0.1	0.1	0.3
Beverages	Ex 111	5.3	4.6	0.5	4.9
Tobacco, unmanufactured	121	539.6	54.5	—	0.2
Hides, skins and furs	21	209.5	54.8	65.0	99.4
Hides and skins	211	152.4	23.3	62.4	96.1
Oilseeds, nuts, etc.	221	871.7	87.4	—	1.6
Soyabeans	221.4	822.3	2.0	—	—
Linseed	221.5	24.0	48.5	—	0.4
Oilseeds nes	221.8	70	37.0	—	—
Natural rubber and gums	231.1	8.1	—	—	—

(Cont'd on p. 65)

APPENDIX 16 *(cont'd)*

	SITC Group or Sub-Group	United States	Canada	New Zealand	Australia
Textile fibres	Ex 26	298.0	2.0	246.2	872.3
Raw wool	262.1, .2	0.3	1.0	246.2	866.8
Raw cotton and linters	263.1, .2	285.7	—	—	5.4
Crude animal and vegetable materials	29	85.5	45.0	24.4	13.6
Crude animal materials	291	21.6	21.2	19.9	9.8
Seeds for planting	292.5	30.9	11.8	4.4	1.6
Animal and vegetable oils and fats	4	307.6	16.3	9.6	21.3
Inedible tallow	411.3	131.6	9.7	9.1	19.7
Processed oils and fats	431	19.3	0.5	0.4	0.8
Essential oils	555.1	30.1	0.7	—	0.6
Casein etc.	599.5	27.1	7.5	28.5	19.2
Total Agricultural Exports		6,029.3	1,151.3[1]	1,031.6	2,242.6

[1]The totals for the United States include re-exports. US Department of Agriculture gives value of 1969 agricultural exports at $US5,936.4m. (Foreign Agricultural Trade of the United States, February 1971).

Source: UN *Commodity Trade Statistics* 1969 (NY, 1970) and UN *1969 World Trade Annual* (Walker & Co., NY, 1970).

COMMENTS BY PROFESSOR K. A. HAY

It is striking that in many places in this paper one could erase 'Australia' and write in 'Canada'. The Australian problem of falling farm incomes exists in many countries with an extensive agricultural base; for example, Japan has imposed severe import controls because of the income problem in the agricultural sector. One important aspect of this is that a country's comparative advantage changes over time. It is now a mistake to say that Canada has a comparative advantage in wheat, for although Canada produces Manitoba number 1 wheat better than anyone else, she charges high prices and thus finds it difficult to sell. Australia is in the same position for some agricultural products, especially wool. In feedstuffs both Canada and Australia now have a comparative advantage. To solve the problems of falling farm incomes and changes in world demand for some fairly staple products like wool or wheat, we must take a longer view of the situation than simply looking for new markets. Development of new agricultural markets may stave off the immediate problem of adjustment but it is not a solution for the essential problem which requires a change in the industrial structure of the country, moving away from dependence on agricultural exports and products toward dependence on other sectors. The costs of this shift will be reflected in a greater exodus of people from the rural areas.

Governments are not very keen on assisting this structural change because of the real political factors involved. They get a good deal of political support from the agricultural sector and in turn they support the agricultural sector far beyond what can be justified on economic grounds. Agriculture obviously has a strategic value and in 10 to 15 years the agricultural sector may be revitalized (possibly in a different form); however, it is most probable that the future of agriculture is not bright and countries such as Australia and Canada must emphasize other industries. In the Canadian west, especially with respect to trade with Japan, the sale of non-renewable resources has taken the place of declining sales of agricultural products and Australia also will likely find itself becoming more and more dependent on this source of income.

In the paper by Sir John Crawford and Professor Board, the Australian rate of growth was estimated at about 5 per cent per year to 1975. This would imply a rising share of imports and along with their concern that Australia's export base is shrinking, they were worried that Australia will become more dependent on foreign capital. However, other alternatives are that Australia could settle for a lower rate of growth or perhaps in the medium term the Australian dollar is overvalued. Australia, faced with contractions in external demand due to the Common Agricultural Policy, the United Kingdom's entry into the European Economic Community and the Green Revolution, is looking for new and expanding markets. Canada is in a similar position, but the Canadian government is placing high hopes on expanded agricultural sales to China; however it is obvious that Canada will not have unique access to China for long.

The other major potential growth market is Japan. Recent events have caught the Japanese growth rate at a lower level than before — I expect it will be roughly 10.8 per cent per year in real terms in the medium term

future. This implies a demand for meat consumption growing at a rate of 14 to 15 per cent per year, using an income elasticity of 1.4. These calculations suggest a substantial potential market even without major changes in Japanese policy. In Japan there are two conflicting factors: on one hand the government wants to protect farm incomes; on the other, the government is worried that the farm sector has contributed substantially to the rate of rise in consumer prices. This problem of maintaining farm income while trying to pursue other economic objectives is replicated in Australia, New Zealand and Canada. Of course the way to suppress these inflationary forces is to open up the economy to more agricultural imports, or, in the case of Japan at least, the revaluation of the yen will lower the price of agricultural imports, giving an even better competitive edge than before. Thus revaluation will have some effect on inflationary pressures but it will aggravate the problem of farm incomes, unless Japan re-imposes strict import controls. This is unlikely, however, since the trend in Japan is to put more emphasis on the quality of life and this means, among other things, higher nutritional levels. Thus, my guess is that as Japan moves from a quantitative view of growth to a more qualitative view, she will allow increases in nutritional levels. If, for example, import controls on beef imports were relaxed, it is apparent from the estimates of price elasticities of demand in Professor D. G. Johnson's paper that the consequent reductions in the price of beef would result in very rapid increases in beef consumption, aside from the income effects.

In relation to the longer range question of restructuring the Japanese agricultural sector, Sir John Crawford and Professor Board mention the Japanese Ministry of Agriculture and Forestry projections to 1977. The Ministry made what seems to be fairly strong assumption about the per cent of food procuded domestically — about 80 to 90 per cent. If import controls based on administrative guidance take this into account, then it is implicit that Japan will import a great deal of feed grain but will suppress imports of meat. However, if a somewhat lower per cent of food produced at home is decided on, then this changes the whole range of possibilities for imports from the Pacific area. There is a tremendous potential for the growth in consumption of food in Japan, a potential which may be met from either of two polar positions — importing feed for cattle or importing carcasses. I suspect that Japan, starting off closer to the first position, will gradually move toward the second, that is, will import more and more meat.

TRADE IN GRAINS AND OTHER CROPS OF EXTENSIVE AGRICULTURE

by

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1. Introduction

The word "extensive agriculture" means types of farming which occur in regions where the man / land ratio is low. Among various types of extensive agriculture, two groups are important in the world: primitive or subsistence agriculture such as nomadism or shifting cultivation; types of farming undertaken in countries of recent settlement.

Countries of recent settlement consist of two groups; developed and less developed countries. Latin American countries were recently settled but are still less developed. Trade in crops produced by primitive extensive agriculture has no importance in the world setting, and we can neglect it in this paper. Crops produced in the recently settled less developed countries such as coffee, cocoa, rubber, cotton and so on are usually called tropical crops, and trade in these crops is worthy of consideration. However, since the cultivation or harvesting of these crops is labour intensive, and since the nature of trade in these crops is quite different from that of grains and other crops, it is better to exclude consideration of trade in these crops from this paper. Agricultural products from the recently settled developed countries are wheat, coarse grains and oil seeds (soybean and rapeseed). Sugar, cotton, tobacco, citrus and other fruits, rice and certain other crops are produced and exported from the recently settled developed countries too. However, these are mainly produced in tropical countries and the products of rather labour intensive agriculture, and we can neglect these in this paper. Crops to be considered in this paper are, therefore, wheat, coarse grains and oil seeds (soybean and rapeseed[1]).

The economic characteristics of these crops are three. First, the production of these crops is the most efficient in world agricultural production. The marketing of these crops is highly efficient too. Efficient animal husbandry has developed upon this efficient economy both in countries that export and import these crops. The share of exports from the United States and Canada of the total world feed grains' exports was more than half in 1951-53 and 1963-65. Western Europe and Japan took 70 percent of the total world feed grains' imports in 1951-53, and 80 percent in 1963-65. Animal industry in these countries is most efficient in the world. Second, the economy of these crops is quite dynamic. The increase in yields per hectare and in labour productivity in producing these crops has increased very rapidly. The development of the soybean industry in the United States which did not exist before World War II has been like that of a mushroom. Japan imported only 1.0 million metric tons of feed grains in 1955. Her imports of feed grains have increased very rapidly since then and she imported 5.6 million metric tons in 1965. Government intervention in the economy of these crops

[1] It is true that oilseeds are produced in tropical countries too, but soybean and rapeseed are mainly produced in the recently settled developed countries.

has been significant both in production and trade. The best examples are the Common Agricultural Policy (CAP) of the European Economic Community, the state trading in wheat, barley and rice in Japan, and the United States grain program.[2] Because of these characteristics, only slight changes in government agricultural programs exert a far-reaching effect upon the welfare of populations both of developed and developing countries.

The purpose of this paper is to examine briefly the nature of trade and trade policy regarding these crops with special reference to trade among Pacific countries. In examining these two fields, the author hopes to suggest something useful in improving trade policies for these crops in Pacific countries.

2. The Background of Pacific Trade with Special Reference to Agricultural Trade

The assertion that an expansion of agricultural trade is needed for a balanced expansion in the world economy can hardly be denied, and the postwar expansion of agricultural trade has been pursued mainly by GATT operations. But during the 1950s it became clear that West European countries were unlikely to open their doors to the agricultural exports from the recently settled countries. Even the United States made it clear that quantitative restriction on imports of dairy products into the United States was necessary. Moreover, the development of the CAP strengthened the protective nature of the agricultural policies of the six countries. It was evident in the late 1950s that the expansion of world trade in agricultural products through GATT negotiations would be extremely difficult.[3]

Governments of importing countries are reluctant to reduce their trade barriers to agricultural products for four reasons. First, the basic structure of peasant-type farming in Western Europe and Japan is extremely deficient when competing with producers in the newly settled countries. Second, in these importing countries, the improvement of the basic structure of production will take many years and huge amounts of government expenditure. Third, farmer's organizations in these importing countries are politically influential. Fourth, not only import barriers into importing countries, but also export subsidies are distorting world trade in agricultural products, and the removal of these export subsidies is also necessary for a reasonable allocation of agricultural resources of the world.

The last point needs further explanation. There are various kinds of measures for agricultural protection. First are measures which restrict imports. These measures are import duties, quantitative restrictions, state trading, multiple exchange rates, state control of the ratio of the mix of domestically produced raw materials with imported materials in processing, commercial agreements with exporting countries and so on. Second are measures which promote exports artificially. Measures under this category are export subsidies, multiple exchange rates, state trading and so on. There is a group of measures which do not interfere with imports or exports direct-

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[2] The general nature of the agricultural programs of these countries is neatly summarized by Mr. Brian Fernon. See Brian Fernon, *Issues in World Farm Trade: Chaos or Co-operation?*, London, 1968, Chap. 4.

[3] Gerard Curzon, *Multilateral Commercial Diplomacy: the general agreement on tariffs and trade and its impact on national commercial policies and techniques*, Geneva 1965, Chap. VII.

ly, but promote domestic production artificially. Measures under this category are direct payment to producers, tax exemption, subsidies on fertilizer, seeds, machines and/or other inputs, and extremely favourable terms of farm loans. These make GATT negotiations in the field of agricultural products extremely difficult and complex. Even after the Kennedy Round, high officials in both the United States and the EEC explained that one of the most important results of the negotiations was that they realized the problems to be solved in improving the world agricultural trade situation.[4] In conclusion, rapid expansion of agricultural trade through GATT operations is not bright.

Among various government measures which distort world trade in crops of extensive agriculture, food aid is worthy of special consideration. This is a kind of subsidized export of food from developed countries to developing countries. (Of course, food aid was given to Western Europe and Japan immediately after World War II.) There are two differences between the usual type of subsidized food exports and food aid. First, food aid is given to developing countries which are permanently or temporally short of food because of foreign exchange shortages. This means that food aid must be an additional import of food into a receiving developing country, and not a substitute for ordinary food imports. In this sense food aid is not a distorting factor of trade in foods. Second, the terms of sale of food aid commodities are concessional, and are not commercial. The terms are sales with a favourable loan rate, sales for local currency and/or gift.

The world total of food aid in 1965 was 1,504.7 million dollars worth of which 1,463.0 million dollars was from the United States, 31.4 million dollars from Canada and 9.9 million dollars from Australia. About 32 percent of the total economic aid of the United States in 1965 was food aid, and about 20 percent of the total economic aid of the OECD/DAC countries in the same year was food aid.[5] This was really a huge amount. Since the main recipients of food aid were Asian countries, and since a large part of food aid has been food grains, including rice, the share of Asian imports in total world food grain imports has increased very much.[6] Especially in the years when India and Pakistan had bad crops, wheat exports under concessional terms from the United States increased very much. For example, in 1966 the United States exported 371 million bushels of wheat under concessional terms. U.S. wheat exports for dollars in the same year was 371 million bushels too. There is no doubt that food aid was an important element in making the world food grain market dynamic.

Crop failures in the Soviet Union in 1963 and in the Indian subcontinent in 1965-67 made the future of the world food situation dark. Already in the early 1960s the future looked less bright since rates of population growth were reaching very high levels. Food grain exporting countries, especially Australia and Canada, increased their acreage under wheat. At the same time both developed and developing countries have concentrated their development assistance and developmental efforts on increasing food grain production in developing countries. The result of these

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[4] Ernest H. Preeg, *Traders and Diplomats: An analysis of the Kennedy Round of Negotiations under the General Agreement on Tariffs and Trade*, Washington, D.C., 1970, p. 158.

[5] Organization for Economic Co-operation and Development, *The Food Problem of Developing Countries*, Paris, 1967, p. 53: —, *Aid to Agriculture in Developing Countries*, Paris 1968, pp. 12-13.

[6] Of course, it should be considered that Japanese imports of wheat has increased very rapidly. Some years ago, China (Mainland) imported huge amount of wheat too.

efforts is the so-called "green revolution" in Asia. Wheat production in India increased from 10.4 million tons in 1966 to 18.6 million tons in 1969, and rice production increased from 45.7 million tons to 61.6 million tons in the same period. Indian cereal imports decreased from 793.0 million dollars worth in 1966 to 376.2 million dollars in 1969. The same was true in Pakistan. Her cereal imports declined from 124.2 million dollars worth in 1965-67 to only 29.5 million dollars in 1969.[7] Since the EEC is becoming more self-sufficient in food grains, Asian countries have been the only increasing importers of food grains in the world. The impact of the "green revolution" on some food grain exporting countries is significant. Australia and Canada reduced their acreage under wheat drastically. The United States reduced her acreage under rice significantly. The future of the world food grain market will be influenced significantly by the future spread of the "green revolution" in developing countries.[8]

There are two types of "green revolution" in Asia. The first is that of India, Pakistan and others. This type of "green revolution" is aiming at self-sufficiency in food grains by various kinds of protective measures, or by import substitution policies. This type of "green revolution" is somewhat questionable if we view it from the point of reasonable allocation of world agricultural resources. The other type is increasing corn production in Thailand. This is a dynamic factor in grain trade in the Pacific.

Another dynamic element in world trade in the crops of extensive agriculture is increased imports of these crops into densely populated industrialized areas in the Far East. The geography of Japan severely limits the land area for cultivation of the crops of extensive agriculture. Acreages under wheat, course grains, soybean and rapeseed have been declining in Japan in recent years. Japan highly protects her agriculture. However, there is no trade barrier to the import of feed grains in Japan since the Japanese government realizes the difficulty of cultivating crops of extensive agriculture. Trade barriers to the imports of oilseeds into Japan are rather nominal. Wheat imports into Japan are under state control. But, compared to protection of rice, Japanese wheat protection has been rather slight. Japanese imports of corn for feed increased by 152 percent between 1960 and 1965, by 25 percent between 1965 and 1969, and by 20 percent in last year. Her soybean imports increased by 110 percent between 1960 and 1965, by 24 percent between 1965 and 1969, and by 31 percent in the last year. Her rapeseed imports have been increasing more rapidly than her soybean imports. Her wheat imports have been increasing slowly in comparison with the imports of the above crops, but wheat imports into the United Kingdom have been stagnant and the EEC's wheat imports have been declining. In Hong Kong and Singapore there is almost no agriculture, and increases in their domestic consumption of grains and oilseeds are completely met by increases in imports. Taiwan and Korea's situations[9] are becoming similar to Japan's.

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[7] These figures are taken from Economic Research Service, U.S. Department of Agriculture, ERS-Foreign 267, *The 1970 Agricultural Data Book for the Far East and Oceania*, November 1970.

[8] For the possible impact of green revolution on the world wheat market, see J. Houck, "The Green Revolution: Its Impact on Trade and Agricultural Policy in Developed Nations", a mimeographed paper presented at a Conference on Agriculture and Economic Development, September 6-10, 1971, Tokyo and Hakone.

[9] For the Korean situation, see Economic Research Service, U.S. Department of Agriculture, ERS-Foreign 306, *Changing Food Consumption Patterns in the Republic of Korea*, December, 1970.

In conclusion, we can point out four background facts. First, the future of a rapid expansion of agricultural trade by thorough GATT operations is not bright. Second, the export of food as food aid was an important element in making the world food grain market dynamic, and food aid is much more important in the Pacific than in the Atlantic. Third, the future of the "green revolution" is crucial in considering future grain trade in the Pacific. Fourth, increase in imports of the crops of extensive agriculture into the densely populated industrialized areas in the Far East is an important dynamic element in the Pacific.

3. Random Elements in Agricultural Policy Decisions

In 1942-43, Dr. Joseph Davis of Stanford University and high officials of the U.S. Department of Agriculture underestimated the post-war relief needs for wheat, and the department launched a wheat-for-feed program. As a result, and with bad weather in Europe in 1945, the United States faced a very serious problem of feeding the world's peoples without sufficient stocks of wheat. The U.S. government therefore encouraged domestic wheat production. In May 1946, the United States Department of Agriculture informed their farmers that the government would pay 30 cents a bushel bonus under the wheat emergency program. In doing so, the U.S. government encouraged wheat production.[10] The United States had already faced a wheat surplus in 1933, and she faced again a more serious wheat surplus problem in the 1950s, and finally launched PL 480. This was an unhappy story, and the main cause was a failure to project future demands for and supplies of wheat.

Japan has now a huge amount of rice surplus and is putting serious pressure both on the world rice market and on the world feed grain market. According to a government source, about a million tons of rice will be used for feed every year for the coming 4-5 years. This is quite unfortunate both for Japan and traditional exporters of rice and feed grains. The story was that in 1961 when the Agricultural Act of 1961 was enacted, the Japanese government intended to adjust Japanese food production to a changing national consumption; that is, we thought that we did not need to produce more rice and that Japan had to produce more vegetables, fruits, milk, meats and so on. However, for political reasons, a bad crop in 1965, and other reasons, the government launched a rice production promotion program in the same year. In launching this program, the government underestimated the declining trend of per capita rice consumption. There is no doubt that this was a mistake, and that the government wasted 10 years in getting its agricultural program going in the right direction.

We are living in a world in which we can not project future demand and supply exactly. A failure in projecting future situations and/or a bad crop directs the government's agricultural policy in a wrong direction. Generally speaking, we were seriously worried about world surpluses of agricultural products in 1950s, and in the early 1960s we were seriously worried about a world shortage of food. The bad crops in the Soviet Union in 1963 and in India in 1965-67 were one of the two main reasons for the pessimism in early 1960s. The other reason was that rates of population growth in less developed countries were made clear in the early 1960s. Once a government adopted a misdirected agricultural policy, its effect on the world market lasts many years since change in agricultural policy is a political affair.

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[10] Don F. Hadwiger, *Federal Wheat Commodity Programs*, Ames, Iowa 1970, Chap. 2.

Another random element in agricultural policy is the CAP. The CAP was not originally designed as a highly protectionist system. However, as Professor Josling pointed out, "the long-term viability of the EEC's common agricultural policy was subordinated to the aim of establishing a Common Policy."[11] Especially when the EEC reached internal agreement on common price levels in a series of marathon sessions during the Kennedy Round negotiations, the common price levels of individual commodities tended to approach the highest individual country level.[12] The CAP owed little to economic practicability and much to political compromise. The result was that the EEC succeeded in solving its internal tensions by making the CAP highly protective.

In examining the future of trade in crops of extensive agriculture in the Pacific, two elements should be considered rather carefully. The one is the problem of projecting future demand for and supply of the crops concerned. There is the "green revolution" in Asia. But we have only insufficient information about the future of the "green revolution". The author hopes that policy-makers in countries of the Pacific are wise enough to distinguish between short-run fluctuations in production and long-run trends in consumption and production, and that we can project future demand for and supply of the crops more exactly.

The other element is political influence. In five developed countries around the Pacific, agriculture is a declining sector of the economy. There is a tendency for the agricultural sector to exert its influence upon their national economic policy-making in a political rather than an economic way. In integrating developed economies around the Pacific, agricultural policy should not be subordinated to political compromise among the countries. They should consider their international responsibility rather seriously, especially their responsibility to the less developed world.[13]

4. Notes on Crops

Feed Grains

As shown in Tables 1-1 and 1-2, feed grain trade is mainly among developed countries. The only exception is the export from Latin America (Argentina) of 1.4 million tons in 1951-53 and 4.8 million tons in 1963-65.

The United States is the world largest exporter. Moreover, her exports increased by 235 percent between 1951-53 and 1963-65, and her exports were almost 47 percent of total world exports. The acreage harvested for major feed grains declined from more than 130 million acres before 1955 to less than 100 million acres after 1964. In spite of this declining in acreage the trend of United states production was upward at a rate of 3.2 million metric tons per year between 1951 and 1969. Therefore, the United States has had a problem of finding a market for her feed grains.[14]

[11] T. E. Josling, *Agriculture and Britain's Trade Policy Dilemma*, Trade Policy Research Centre, London, 1970, p. 2.

[12] H. B. Malmgren and D. L. Schlechty, "Technology and Neo-Mercantilism in International Agricultural Trade", in *American Journal of Agricultural Economics*, December, 1969, p. 1327.

[13] While demanding that Japan take down its barriers to agricultural products, the developed countries which export agricultural products should very seriously take into consideration the needs of the Southeast Asian less developed countries.

[14] It is interesting to note that an authoritative study about grain yields in the United States done in 1962 did not expect such an increase in United States productive capacity. See D. Gale Johnson and Robert L. Gustafson, *Grain Yields and the American Food Supply: An Analysis of Yield Changes and Possibilities*, Chicago, 1962.

There has been a vast idle capacity of feed grain production in the United States. Australia and Thailand have expanded their exports rapidly too. Their exports are expected to increase in future since Japan has planned to diversify her source of feed grain imports, and since there is capacity to increase feed grains production in both countries. In 1951-53 Canada was the second largest exporter of feed grains, but her exports declined by 56.5 percent in the following 12 years. Nearly all of the decrease resulted from lower exports to the United States. In 1951-53 about 50 percent of Canadian exports went to the United States, but in 1963-65 it was only 10 percent.

The EEC is the world largest importing region for feed grains followed by Japan, the United Kingdom and the rest of Western Europe. Japanese imports increased most rapidly, and her feed grain imports in 1963-65 was almost five times her imports in 1951-53. EEC imports increased very much too. However, it should be noted that EEC exports increased tremendously. It is expected that Japan is likely to at least double her import of coarse grain to over 10 million tons in 1980 while the EEC is expected to continue importing at about the present rate of 13 million tons, though slight deviation from projected meat demand would cause EEC imports to double by 1980.[15] The acreage under coarse grains has not changed since the early 1950s. Production, however, increased rather steadly as a result of increase in yields. In 1967 and 1968, production of feed grains was particularly high in the EEC and imports dropped. The reason for these changes were very large increase in yields in both years. On the consumption side, it is likely that non-grain feed, such as potatoes for hogs, will decline. However, with the rise in prices of feed grains by the CAP, EEC countries such as the Netherlands have increased their imports of non-grain feeds such as cassava meal.[16] Future feed grain imports into the EEC are quite uncertain. The United Kingdom and the rest of Western Europe are the world's biggest importers. The United Kingdom's imports have been rather stagnant while the net import of feed grains by the rest of Western Europe has increased more rapidly than imports to the EEC. It is expected that EFTA and Western European nations will increase their imports by 60% over 1965, and will import 8 million tons of feed grains in 1980.

There are many uncertain elements in the world coarse grain market including the future of Communist Asian imports which have been and will be almost self-sufficient in coarse grains. Generally speaking, however, the world feed grain market has been and will be much more dynamic than that of wheat. The most dynamic element in the world feed grain market has been and will be imports into Japan.

Wheat

There have been considerable changes in the world wheat economy since the end of World War II. Moreover, there have been considerable differences both in rates of increase in production and consumption among regions of the world. As a result, patterns of the world wheat trade changed.

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[15] These figures are quoted from Foreign Agricultural Economic Report No. 63, U.S. Department of Agriculture, *Growth in World Demand for Feed Grains Related to Meat and Livestock Products and Human Consumption of Grain: 1980*, July 1970.

[16] See, Economic Research Service, U.S. Department of Agriculture, ERS-Foreign 287, *The Netherlands' Mixed Feed Industry, its impact on use of grain for feed*, May 1970.

TABLE 1-1.

Feed Grain Imports by Importing Regions,
Averages 1951-53 and 1963-65

	1951-53 Average	1963-65 Average	Percentage Change
	..... 1,000 m.t.		
Developed countries			
EEC	4,787	14,302	198.8
Other Western Europe	1,923	4,808	150.0
Japan	976	4,657	377.2
U.K.	2,771	4,150	49.8
Canada	154	373	142.2
U.S.	1,678	189	-88.7
Australia, New Zealand and South Africa	99	2	-98.0
Total	12,389	28,487	129.9
Centrally planned countries			
Total	740	3,368	355.1
Less developed countries			
East Asia	308	361	17.2
South Asia	618	143	-76.9
Southeast Asia	.....	16	.....
Total	1,582	2,781	75.8
World total	14,705	34,632	135.5

Source: Foreign Agricultural Economic Report No. 63, U.S. Department of Agriculture, *Growth in World Demand for Feed Grains Related to Meat and Livestock Products and Human Consumption of Grain: 1980*, July 1970, p. 4.

TABLE 1-2.

Feed Grain Exports by Major Exporters,
Averages 1951-53 and 1963-65

	1951-53 Average	1963-65 Average	Percentage Change
	..... 1,000 m.t.		
Developed countries			
U.S.	4,817	16,155	235.4
EEC	187	3,833	*1)*
Australia, New Zealand and South Africa	729	2,102	188.3
Canada	3,198	1,390	-56.5
Other Western Europe	313	541	72.8
U.K.	91	187	105.5
Japan	33	.....	.....
Total	9,369	24,208	158.4
Centrally planned countries			
Total	2,122	3,601	69.1
Less developed countries			
Southeast Asia	61	964	*1)*
South Asia	.....	79	.....
Total	3,218	6,822	137.2
World total	14,709	34,631	135.5

Source: Foreign Agricultural Economic Report No. 63, U.S. Department of Agriculture, *Growth in World Demand for Feed Grains Related to Meat and Livestock Products and Human Consumption of Grain: 1980*, July 1970, p. 5

1) Base too small to compute meaningful percentage change.

World wheat production increased by 48 percent from 179.7 million tons in 1949/50-1952/53 to 266.4 million tons in 1962/63-1966/67.[17] About half of this increase was in Soviet Union and Eastern Europe. Western Europe increased its wheat production from 31 million tons to 46 million tons during the same period. About two thirds of this increase occurred in countries that were traditional importers, and their wheat imports declined. Traditional exporters (North America and Australia) did not increase their wheat production until 1956/57-1958/59. However, their wheat production increased very much thereafter. From 1956/57-1958/59 to 1962/63 — 1966/67, wheat production in North and Central America increased by 9.1 million tons, and in Australia by 5.5 million tons. These areas also increased their wheat exports very much during the period.

World wheat imports increased by more than 100 percent from 25.3 million tons in 1949/50-1952/53 to 53.3 million tons in 1962/63-1966/67. The share of Western European wheat imports in world total import declined from about half to 22 percent during the same period while that of the centrally planned countries increased from almost none to 30 percent during the period. Asia (excluding Mainland China) increased its wheat imports from 6.1 million tons to 15.8 million tons during the same period. Asian imports were mainly from the United States, and a large part was on concessional terms. Generally speaking, the imports of the centrally planned countries were not from the United States.

In recent years both centrally planned countries and Asia have increased their wheat production either by new agricultural programs and/or the "green revolution", and the impact of these changes on world wheat trade is serious. Australia and Canada have much decreased their acreage under wheat. Future prospects for the world wheat economy seem serious as shown in Table 2.

Oil Seeds

Except for the United States, developed countries are importers of oilseeds and oilseed products. The United States is the world biggest exporter of oilseeds and oilseed products. Less developed countries are, generally speaking, exporters of oilseeds and oilseed products. (See Table 3)

World trade in oilseeds and oilseed products has been and will increase since consumption is increasing both in developed and less developed countries. In developed countries the main increase will be in oilcake while in less developed countries the main increase will be in vegetable oils. It is generally projected that oilcake prices in 1980 will be higher than in 1963-65, while vegetable oil prices in 1980 will be lower than in 1963-65.[18] Japan will continue to increase her imports. The United States will continue to increase her exports. Canada will be an exporter of vegetable oils in 1980 while she will continue to be an importer of oilcake in 1980.

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[17] These and following figures are taken from P. A. Westerman, "Change in the World Wheat Situation and the 1967 International Grains Arrangement", in the *Quarterly Review of Agricultural Economics*, Vol. XXI, No. 2, 1968.

[18] Since there are a great many varieties in oilseeds and vegetable oils, the author does not go into the details. For details see, Foreign Agricultural Report No. 71 U.S. Department of Agriculture, *World Supply and Demand Prospects for Oilseeds and Oilseed Products in 1980*, March 1971.

TABLE 2

Production, Domestic Disappearance, and Net Imports of Wheat, by Regions, Average 1964/65—1966/67 and Projected 1980/81 (1,000 metric tons)

	1964/65—1966/67			1980/81		
Region	Production	Domestic Disappearance	Net Imports	Production	Domestic Disappearance	Net Imports
Developed	109,260	78,781	-32,958	143,514	87,720	-55,794
Centrally Planned	106,848	120,693	13,845	146,148	150,960	4,812
Less Developed	46,980	66,254	18,194	87,501	116,460	28,959
Total World	263,088	265,728	-919	377,163	355,140	-22,023

Source: Quentin West, "World Grain Production Prospects and Trade Stabilization Measures in Southeast Asia", in *Agricultural Revolution in Southeast Asia: Impact on Grain Production and Trade*, Vol. 1, New York, 1970, p. 155.

TABLE 3

World Trade in Oilseeds and Oilseed Products, 1963-66 Average. (1,000 dollars)

	Net Trade			
	Oilseeds	Vegetable Oil	Oilseed Meal	Total
United States	578,295	117,475	168,608	864,379
Canada	-20,830	-15,545	3,033	-33,341
EEC	-618,712	-125,939	-248,399	-993,050
United Kingdom	-115,192	-72,005	-105,004	-292,201
Other European Countries	-166,018	-29,230	-131,589	-326,837
Japan	-272,669	-3,434	-7,345	-283,448
Australia-New Zealand	-9,265	-10,946	-1,231	-20,942
South Africa	9,200	-850	-11	8,339
Total	-615,191	-140,474	-321,938	-1,077,101
Centrally Planned Countries	41,239	30,677	-35,512	36,405
Less Developed Countries	491,551	171,033	260,865	923,450
World Total	-82,401	61,236	-96,585	-117,247

Source: Foreign Agricultural Economic Report No. 71, U.S. Department of Agriculture, *World Supply and Demand Prospects for Oilseeds and Oilseed Products in 1980*, March 1971, p. 13.

AGRICULTURAL PRICE POLICIES AND EFFECTS ON TRADE: SOME EXAMPLES FROM THE UNITED STATES AND WESTERN EUROPE

by

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Several years ago I argued that the agricultural trade policies of the industrial countries could be accurately described as the New Corn Laws. The British Corn Laws included every feature that is now included in the Common Agricultural Policy of the European Economic Community or in the restrictive trade programs of the United States except for deficiency payments. The variable levy is not the invention of the EEC; it probably came from some fertile British mind in the 17th century. Export subsidies or bounties have an even more ancient origin and they had an important role in the British Corn Laws. And perhaps equally striking the rationale for the British Corn Laws bears more than a passing ressemblance to the reasons now given for the need for agricultural protection in the industrial countries:[1]

> "Whereas the labourers and occupiers of husbandry within this realm be daily grievously endangered by bringing in of corn out of other lands and parts into this realm, when corn of the growing of this realm is at a low price"; (no corn was to be imported if the prices of grain were below specified minimums). 1463
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> "Forasmuch as the encouragement of tillage ought to be in an especial manner regarded and endeavored; and the surest and effectual means of promoting or advancing any trade, occupation or mystery, being by rendering it profitable to the users thereof; (2) and great quantities of land within this kingdom for the present lying in a manner waste, and yielding little, which might thereby be improved to considerable profit and advantage (if sufficient encouragement were given for laying out cost and labour on the same), and thereby much more corn produced great numbers of people, horses and cattle employed, and other lands also rendered more valuable." 1663
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> "Forasmuch as it hath been found by experience, that the exportation of corn and grain into foreign parts, when the price thereof is at a low rate in this kingdom, hath been a great advantage, not only to the owners of land, but to the trade of this kingdom in general . . . ." 1688. (This act was probably the first act providing for export bounties and it is said that precautions were taken to prevent the subsidized corn from being reshipped back into Great Britain.)
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> "Whereas a great deal of the richest and best land of this kingdom is and cannot so well be otherwise employed and made use of as in the feeding and fattening of cattle, and that the coming in of late of vast numbers of cattle already fatted, such lands are in many places much fallen, and likely daily to fall more in their rents and values, and in consequence other lands also, to the great prejudice, detriment, and impoverishment of this kingdom . . ." 1663. (The act included provision for import duties to be applied seasonally — a relatively high duty when British fat cattle were marketed and free trade the rest of the year — and an import quota on cattle imported from the Isle of Man.)

But there is a difference of degree, if not of kind, in the objectives of the new and old corn laws. While in the formulation of the British Corn Laws there was concern about the effects of low farm prices upon employment (men, horses and cattle), land rent and general prosperity, the new corn

[1] Quotations from and explanatory material based on Cornelius Walford, "The Famines of the World: Past and Present — Part II," *Journal of the Royal Statistical Society*, Vol. XLII, March, 1879, pp. 133-38.

laws emphasize an income objective even though there is often considerable embiguity about the specific definition of that objective. The new corn laws place emphasis upon the relative incomes of the farm and nonfarm populations.

In its highly useful summary, *Agricultural Policies in 1966*, the OECD staff states the following:[2] "The main objectives of most governments in their agricultural policies continue to be to support farm incomes, adjust production to outlets and ensure supplies at reasonable prices to consumers. . . . The aim of improving farm income levels is set out in legislation, or in official statements of policy, in the majority of countries. The income level aimed at is defined in various ways, often by reference to incomes in other sectors. Thus the aim may be to ensure for those engaged in agriculture a 'fair' or 'proper' remuneration (as in the Netherlands, the United Kingdom, and the Treaty of Rome), to enable them to participate in the general improvement of incomes or living standards (Austria, Germany, Sweden), to reduce the income gap between agriculture and other sectors (Italy), or to ensure farm incomes comparable with those in other occupations (Finland, France, Iceland, Japan, Luxemberg, Norway, Switzerland)."[3]

Trade restrictions and interferences for agricultural products in the industrial countries are only one set of means used to achieve one or more of the various income objectives. In fact, in most cases such restrictions and interferences are simply adjuncts to the price and subsidy policies that are supposed to increase the returns to farm resources. It is this close tie between domestic farm policies and trade policies for farm products that makes it so difficult to negotiate meaningful changes in agricultural trade restrictions. All too often the governments of industrial countries look upon discussion of their agricultural trade policies as an attempt to interfere in their domestic policies and politics.

But the main point I want to make in these introductory remarks, before turning to an examination of certain trade effects, is that there is little evidence that the farm policies now being followed in the industrial countries have made or can make any significant contribution toward increasing the returns to human resources in agriculture relative to what comparable resources earn in the rest of the economy. Some contribution can perhaps be made toward reducing the disparity between the incomes of the farm and nonfarm populations, since the high price supports and subsidies do result in an increase in the return to land. But the increase in land return makes little long run contribution to the solution of income problems that confront farm people in the industrial countries. In fact, higher land values can complicate

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[2]OECD, *Agricultural Policies in 1966* (Paris, 1967), p. 59.

[3]The continuing discussion (*ibid.*) is of interest: "In several cases these income objectives are qualified or accompanied by references to the need for a satisfactory level of productivity in agriculture, and sometimes they relate specifically to farms meeting certain standards of efficiency: thus in Belgium the aim is to ensure the profitability of holdings which are well managed and whose existence is economically and socially justified; in Finland, farms with a 'satisfactory degree of rationalization' should have incomes corresponding to those of other economic groups; in Sweden the size of farm to be used in income comparisons is laid down; in Switzerland a fair remuneration for farmers is to be ensured through prices covering average production costs on rationally operated farms; in the United States the objective is to provide opportunity for the efficient family farmer to earn 'parity of income from farming operations' and to provide 'parity of opportunity' for all rural people, including small farmers; in some cases income comparisons are made with specified non-farm groups (wage-earners in comparable non-agricultural occupations in Germany, certain groups of industrial workers in low-cost living areas in Sweden, non-farm workers in rural and semi-urban districts in Switzerland)."

the problems of adjustments that all farm people must make to the process of economic growth; high land prices makes it more difficult to enlarge farms and induce expenditures upon resources that substitute for land. High land prices by inducing expenditures upon land substitutes add resources to agriculture when at the same time it is necessary for labor employment to decline unless returns to farm labor are to decline relative to the return to nonfarm labor of comparable skills and capacities. It is quite common for the agricultural programs of the industrial countries to subsidize nonlabor inputs in guise of improving the structure of agriculture. Both the high land prices and the subsidies for buildings, land consolidation and farm rationalization either directly reduce the returns to farm labor through effects on farm prices or increase the costs of maintaining a given level of farm output prices.

It is not uncommon for some of us who are of European origin to speak derisively of the sacred cows of India and to point out all of the benefits that would flow from more rational attitudes toward this animal. Without attempting to discuss either the empirical validity of the presumed status of cows in India or the effects of changes in that status, it is unlikely that the cow is any more sacred in Indian life than is the dairy cow in the political life of Western Europe, the United States, the United Kingdom, Canada or Australia. Whatever the consequences of the sacredness of cows in India, it is all too clear what are the major consequences of its peculiar attraction for policy makers in the major Western industrial countries.

In the United States the dairy cow is responsible for one of the two most egregious departures from liberal trade policies affecting agricultural products; in Australia that must export farm products in order to survive the dairy cow has resulted in a series of trade interfering devices and in the EEC the dairy cow has induced otherwise frugal politicians to expend almost a billion dollars annually in recent years. And as so often happens in our efforts to protect our gods, or more accurately, our goddesses, we take measures that will eventually destroy them. In the case of several industrial countries butter has already been priced into eventual virtual extinction; if present trends continue by the end of this century butter will no longer be a common consumer item.

The sacred role of the dairy cow not only pollutes the relations among nations because of the restrictions on and interferences with trade in dairy products, but also through the effects on trade in beef. If the United States did not go to such lengths to protect its dairy industry, it would hardly be concerned with either voluntary or mandatory controls on beef and veal imports. Similarly in the EEC and other Western European countries, if dairy product prices were not so high — and so much beef and veal produced as a by-product — beef imports would be substantially greater.

There is another sacred object in most of the industrial countries though it is not certain whether it is worshipped openly and knowingly or is so subtle in its effects on man's mind that its sacred position is reflected solely in subconscious behavior. I refer to farm land. In the long run almost all of the net benefits of the very costly farm programs of the industrial countries are absorbed through higher land prices. A sacred object that can induce governments to commit their citizens to annual expenditures of about $40 billion must have great attractions and powers. And it is a sacred object that a few economists are not going to be able to displace from its position easily.

In this paper the emphasis will be upon trade and agricultural products that affect livestock products. In fact, primary attention is given to dairy products and beef and veal since these are the major animal products seriously affected by trade restraints and interferences. Poultry meat — especially broilers — might have been added to this list. However, it is of primary concern to only one country in the Pacific area and the major trade restraints occur in Western Europe and thus it has been touched upon only in passing.

Dairy Products

With the exception of New Zealand, all of the high income countries of the world interfere with the market prices of dairy products and even New Zealand isn't above a little tinkering in the name of price stabilization. In addition to New Zealand, three other countries in the Pacific Region and Western Europe have moderately reasonable dairy product prices in the range of $6-8 per 100 kilograms — Denmark, Ireland and Australia. In the general range of $8-10, one finds the United Kingdom, Austria, France, Belgium, Canada, and the Netherlands; between $10-12 are Germany, Italy, Sweden, Switzerland, and the United States. Japan and Norway have producer prices for milk in excess of $12 per 100 kiligrams.

The high prices for dairy products have three main effects upon international trade: (1) Reduces imports of dairy products due to effects on domestic consumption and production; (2) Results in a substantial flow of heavily subsidized exports of dairy products from the high cost countries; and (3) Increases the supply of beef and thus reduces the amount and value of international trade in beef that is based on an economically rational allocation of resources. The third of these effects will be considered in the next section of this paper.

The OECD countries produced 186 million tons of milk in 1968. To one degree or another all of this milk production involved some subsidy or trade protection; about 9 million tons — the production in Denmark and Ireland — was produced with what could be called a moderate degree of nominal protection. The milk output in New Zealand in 1968 was approximately 6 million tons — the only milk produced in the OECD plus Oceania that has no significant nominal protection. Australia produced 7 million tons and did so under conditions involving government subsidies and price discrimination against local consumers. However, while there is validity to the claim made by U.S. dairy producers that imports of dairy products from Australia are available because of export and other subsidies, the average return per unit of milk produced by the Australian farmer is only a little more than half that received by U.S. farmers.

Thus of the total OECD plus Oceania milk production of about 200 million tons only a little more than 10 percent is produced without significant protection. In terms of estimating the effects of protection on consumption, one could add the United Kingdom's 13 million tons. The only reasonably open market for manufactured dairy products in the world is provided by the United Kingdom, though this is apparently about to pass into history along with the hula hoop and silent movies. If imported processed products are converted into whole milk, the United Kingdom imports about half of its total milk supply. In 1967/68 the United Kingdom was responsible for almost two thirds of the world's imports of butter and about a quarter of all cheese imports. It maintains an import quota on butter and participates in voluntary restraints on cheese imports. But these arrange-

ments appear to be primarily designed to protect its traditional suppliers — New Zealand, Australia and Denmark — from the heavily subsidized exports from the EEC. Without these controls the British market would be flooded with butter and cheese produced under high cost conditions. In 1968 the EEC paid an export subsidy on butter exported to the UK that was about 150 percent greater than the London market price for butter. With competition like that the traditional exporters obviously require assistance from some source.

The milk producer in the United Kingdom is not without friends in court. Returns to producers are maintained by discriminatory pricing practises that result in prices paid for milk used for fluid purposes (about two thirds of UK production) that are about 2.5 times the price paid for milk for manufacturing purposes. The producer is then paid an average or blend price that is less than 10 percent below the average EEC producer price. If there is a loser, it is the consumer though he has gained from having the lowest prices for manufactured milk products available in any industrial country.

What have been the consumption effects of the high consumer prices for at least 80 percent of the milk consumed in the OECD plus Oceania? This is not a simple question since we do not know how much recent prices have departed from what prices would be if there were free trade in dairy products. Do we assume that there would also be free trade in grains and feeds? Part of the high cost of dairy products in the EEC, though not in the United States or Canada, is due to high feed prices and high land prices resulting from the grain price policies of the EEC. Nor do we have very much reliable knowledge of the price elasticities of demand for milk products though Brandow's work for the United States can probably be used to give a *lower* limit for the effects of price on consumption. He has obtained the following estimates of price elasticities of retail demand for milk products in the United States: Fluid milk and cream, -0.28; butter, -0.85; cheese, -0.70; ice cream, -0.55.[4] The elasticities at the farm level were substantially lower, averaging about a half of those indicated above. The largest use of milk is for fluid milk and cream and this has the lowest price elasticity. If we assume that the weighted price elasticity of demand at retail is -0.35, that the reduction in retail prices is one half that at the farm level, and that farm prices of milk products were reduced by 20 percent for 80 percent of total consumption, the consumption of milk products in the OECD plus Oceanis would increase by about 3 percent or 6 million tons.

The 20 percent reduction in farm prices in the present high price areas is an arbitrary assumption and would result in reducing average producer prices from about $10-11 per 100 kilograms to about $8-9 in all the area outside of Oceania, Denmark, Ireland and the United Kingdom. Note that the increase in consumption, under these assumptions, is about a fourth of current total production in Oceania, Ireland and Denmark — the low cost producers. The United Kingdom is not included in this group because it has producer prices almost as high as those in the EEC but with much lower feed prices than the EEC.

The supply effect of the protection of milk production is probably rather more conjectural than the consumption effect because of the greater

[4]George Brandow, *Interrelationships Among Demands for Farm Products and Implications for Control of Market Supply*, Pennsylvania State University, Agricultural Experiment Station Bulletin 680 (1961), p. 13.

analytical and statistical problems of estimating the price elasticities of supply for dairy products. But there are a number of such estimates that can be used to arrive orders of magnitude, at least. Tweeten has estimated that the intermediate run (two year) price elasticity of milk output in the United States to be 0.3.[5] Gruen has estimated that the short run (one year) price elasticity of milk output is 0.20 and the intermediate run (five year) elasticity was 0.43.[6] George Jones has made estimates of the effect of changes in various prices upon milk output or a proxy for milk output for the United Kingdom and the EEC. Jones has estimated that the long run elasticity of the number of cows in the United Kingdom with respect to the price of milk is between 0.27 and 0.47 (short run elasticities of 0.17 to 0.23).[7] Since the number of all cows and not just dairy cows is used as the dependent variable and no effect of prices on milk yield per cow is included, the supply response estimates are on the low side as a measure of the price elasticity of milk output.

Jones kindly made some unpublished estimates of milk supply response for the EEC available to me. He has obtained an estimate of 0.57 for the long run; this elasticity assumes that all other prices are constant, it should be noted.

If the estimates of supply elasticities are accepted as ranging from 0.3 to 0.5, we can indicate the effect of a 20 percent reduction in dairy product prices (holding the price of beef and feed constant) upon production of milk in the OECD plus Oceania. Note that this price reduction applies to 80 percent of the total milk output. The output reduction would range from a low of 10 million tons to a high of 16 million tons. The sum of the output and consumption effects would be approximately 16 to 22 million tons or from 8 to 11 percent of the current output in the regions under consideration. On a butterfat basis (assuming a fat content of 3.5 percent) the reduced consumption plus increased production is estimated to be 580 to 770 thousand tons. In 1961-63 the total of exports of all milk products, in terms of butterfat, from Denmark, Ireland, Australia and New Zealand was 420 thousand tons.[8] Thus the effect of a 20 percent reduction in farm dairy product prices would result in a substantial expansion of unsubsidized trade in dairy products and a very significant increase in the prices at which dairy products would move in international trade.

The trade restrictions that have been used in the OECD to buttress domestic price policies for dairy products have clearly reduced the flow of trade between low cost and high cost dairy producing areas. The high consumer prices, except in the United Kingdom, have also reduced consumption by an amount that is large relative to international trade in dairy products. In addition a significant part of the total exports of dairy products from the OECD countries are either subsidized (EEC, Switzerland, Norway, Sweden) or sold on non-commercial terms (United States).

I will conclude this discussion of the effects of lower dairy product prices by a brief comment on the probable level of milk production in the

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[5]Luther Tweeten, *Foundations of Farm Policy* (Lincoln, 1970), p. 243.
[6]F. H. Gruen, *et al., Long Term Agricultural Supply and Demand Projections, Australia, 1965 to 1980* (Monash University, Australia, 1968), p. 178.
[7]George Jones, "The Influence of Price on Livestock Population Over the Last Decade," paper circulated in advance of the annual meeting of the British Agricultural Economics Society (July, 1965), p. 22.
[8]OECD, *Agricultural Projections for 1975 and 1985, Europe, North America, Japan, Oceania* (Paris, 1968), p. 38.

United States if the price supports were removed and the import quotas abandoned but the existing tariffs were retained. Under these circumstances I believe that the United States would produce only enough milk for fluid consumption as milk and cream — about 25 million tons — and the amount of manufactured products that would be required to provide an adequate supply of milk for fluid consumption. Because of seasonal variations in milk production and year to year fluctuations because of weather conditions, the additional production for manufactured purposes might be 50 percent of the amount used for fluid purposes or about 12.5 million tons. In 1970 total U.S. milk production was 53 million tons. If fluid use remained constant — it appears to be declining slowly — output would be reduced by about 16 million tons.

This reduction is somewhat larger than is implied by a price elasticity of supply of 0.3 to 0.5, unless the reduction in producer price exceeds 60 percent. The reduction that I have estimated in this subjective way would probably occur if the prices of manufactured milk products in the United States fell by 20 to 25 percent from their present levels. Even though the relative price of milk to the price of dairy feed has increased by about 15 percent since 1963 and 1964, milk production declined by about 8 percent between 1964 and 1970. Over the same period the absolute price of milk increased by 38 percent, though the real price increased by less than 15 percent. Labor requirements in dairy production are simply too high in the United States to make the industry competitive.[9]

Beef and Veal

In 1968 or 1968/69 producer prices for beef cattle (per 100 kilograms of liveweight) varied almost as much in the major producing regions as did milk prices. In two countries — Argentina and New Zealand — producers got less than $30; in Australia, Denmark and Yugoslavia the price was between $30 and $40; in Ireland and the United Kingdom, between $40 and $50; in Canada, the United States, Norway and Spain, between $50 and $60 (though the U.S. and Canadian prices were just at $50); the EEC and Sweden, at $60-$70 except Italy was just over $70, and the USSR topped the list with a farm price in excess of $130. Obviously quality differentials are much more important than for milk. For example in the Chicago market in 1968 the average price for all steers was $61 per 100 kilograms compared to $38 for commercial cows, roughly the average for cows discarded from dairy herds. Approximately the same difference would exist in Canada. On a quality adjusted basis the prices for cattle in the U.S. and

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[9]The following tabulation gives labor requirements per unit of output and prices per unit of output, both relative to dairy products, for several farm products:

	Relative Labor Requirements 1964-68	Relative Farm Prices, 1967
Milk	100	100
Beef	220	440
Pork	150	380
Broilers	60	270
Corn	80	230
Soybeans	190	520

Source: USDA, *Agricultural statistics, 1969*, pp. 458 and 463-65.

Obviously inputs other than labor are required for the production of these farm products, but the steady increase in the real price of labor has undoubtedly been a significant factor in the different output growth patterns.

Canada are probably lower than those in Ireland and the United Kingdom though above the prices in Australia and Denmark. And certainly on a basis adjusted for quality the beef prices paid to producers in the EEC and Sweden are substantially greater than in the British Isles or North America.

World trade in beef and veal in 1966 amounted to about 4 percent of estimated world production.[10] Most of the imports are accounted for by the United States, the EEC and the United Kingdom and most of the exports by Australia, New Zealand, Argentina and Denmark.

Trade in beef and veal is much affected by a variety of trade, sanitary, and health regulations. The EEC maintains a difference of approximately 50 to 70 percent between domestic and import prices of beef. The United States controls the importation of certain types of beef and veal through so-called voluntary agreements with its major suppliers, but the volunteerism is strongly supported by the threat of imposition of import quotas under the Meat Import Act of 1964. The U.S. tariff duty on fresh, chilled or frozen beef and veal is relatively low at 3 cents per pound or about 6 percent. On canned beef the tariff rate is 7.5 percent; on corned beef hash it is 10 percent.

How much have the import restrictions on beef reduced U.S. imports of beef over the past few years? Brian Fernon has concluded:[11] "Free trade would probably have little effect on the demand for beef imports by either the United States or Canada, or on the border trade between the two countries which is based largely on seasonality of supplies." Earlier Fernon has said: "Australia and New Zealand produce beef at considerable lower prices than Northern Hemisphere countries. Free trade would not, however, enable them swiftly to replace domestic production in those countries, since consumers generally prefer fresh home-grown beef to frozen imports from Australia and New Zealand and seem prepared to pay a premium for it. American restrictions, consisting of a relatively low tariff and an import quota covering beef, veal, mutton and goat meat, did not seem greatly to inhibit imports until the last years of the 1960s. Before that imports were not available in sufficient quantities to make the quota applicable."

The first year that the import quota and the voluntary agreements that have been used to support it had any significant effect on imports was probably 1969 when imports of meats subject to the quota were almost identical to the quota. In 1970 such imports exceeded the quota by almost 7 percent and I assume might have gone somewhat higher in the absence of the import quota. The size of the import quota increases with the growth in U.S. consumption of the products involved and since the base was established in 1964, the base grew by 37 percent by 1970.

U.S. imports of Australian and New Zealand beef are used primarily for manufacturing purposes — sausage, hamburger and TV dinners. The imports are thus primarily competitive with the lower grades of beef and not with fed beef. An important factor in the rapid expansion of such imports has been a significant change in the composition of U.S. cattle production and slaughter. In 1956 almost 31 percent of U.S. cattle slaughter was cow slaughter; by 1969 this percentage had dropped to 19 percent. Or looked at another way, the three lowest grades of beef accounted for 42 percent of

[10] Brian Fernon, *Issues in World Farm Trade: Chaos or Co-operation*, Trade Policy Research Center, London, 1970, p. 129.
[11] *Ibid.*, p. 81.

total slaughter in 1956 and 19 percent in 1969. Thus beef imports have increased quite rapidly primarily in response to changes in the quality or grade composition of U.S. beef slaughter and, to some degree, the amazing and increasing popularity of the hamburger.

Total exports of beef and veal from New Zealand and Australia in 1963 were 88 percent of U.S. imports in that year; U.S. imports declined in 1964 while the exports from Oceania remained approximately unchanged and their exports were 128 percent of U.S. imports. In 1965 the exports of the two countries rose to 167 percent of U.S. imports as U.S. imports declined further. U.S. imports increased in 1966 and again in 1967; the ratio of exports from Oceania to U.S. imports were 109 and 97 percent, respectively. Between 1967 and 1969 U.S. imports increased from 382,000 tons to 470,000 tons and the Oceania exports were 88 percent of U.S. imports in 1968 and 97 percent in 1969; during the first half of 1970 the percentages remained unchanged at the 1969 level. The quota restrictions were without effect from 1963 through 1968. While not much can be inferred from the above comparison of Oceania exports and U.S. imports, it might be concluded that the restraining effect upon exports from Oceania was relatively small in both 1969 and 1970. By relatively small, I mean that it was almost certainly less than a fourth and probably as small as a tenth or less than 50,000 tons.

Even if the quota has had little effect on imports, I still feel that the quota arrangement should be abolished. The only bright side of the picture is that because there is a quota the 10 percent import surcharge has not been applied to meats subject to the quota.

The major element in the reduction of international trade in beef and veal is, without doubt, the subsidization of dairy production in Western Europe and North America. If U.S. dairy production declined by a third, as it would if there were only a moderate degree of protection, the reduction in beef and veal production from the 1970 level would be at least 500,000 tons (carcass weight); this is approximately three fourths of all U.S. imports of beef and veal in that year. If dairy production were not subsidized in Western Europe the effect on beef and veal production would be much greater. The reason is not the higher degree of protection in Western Europe than in the United States, but the much greater relative importance of the dairy herd as a source of beef and veal. Fernon estimates that in the United Kingdom that the dairy herd is responsible for about three fourths of beef and veal production.[12] It is probable that for the rest of Western Europe the dairy herd provides an even larger fraction of the total beef and veal supply.

Production of beef and veal in Western Europe is now about 6 million tons. If 80 percent of this total is a joint product with dairy, each 10 percent reduction in milk production would reduce beef and veal production by 500,000 tons.[13] Thus if the elimination of protection for dairy production were to reduce milk production by 20 percent in Western Europe, meat production might be reduced by 1 million tons. I do not know if a 20 per-

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[12] Fernon, *op. cit.*, p. 83.

[13] It should be noted that if milk production declined by 10 percent that beef and veal production could decrease by either more or less than the amount indicated because of changes in factor prices and other product prices that would occur as a result of the change in milk prices associated with the decline in milk output. It is probable that the decline in beef and veal production would be somewhat less than that indicated *if* beef and veal prices remained unchanged because of the decline in forage prices or costs.

cent reduction in milk production under approximate free trade conditions is a realistic estimate or not; it would be consistent with a long run elasticity of supply of 0.5 and a 40 percent reduction in the price of milk. But even if the reduction in milk production were only 10 percent, the decline in beef and veal production would be 500,000 tons. Combined with the estimated reduction in beef and veal in the United States, the reduction in the two areas might be put at 1 million tons. This compares with the 1968 total production of beef and veal in Australia and New Zealand of 1.25 million tons.

A second factor in the reduction of international trade in beef and veal are the high consumer prices in Western Europe, except for the United Kingdom and Ireland. The price elasticity of demand for beef and veal is relatively high, at least compared to other farm products. It is probably at least -0.6 for the high income countries. Thus high beef prices in major importing countries have had a significant effect on consumption. If EEC retail prices of beef have been increased by a third,[14] this means that consumption per capita has been reduced by about 20 percent. In 1969 beef and veal consumption totaled 4.5 million tons;[15] at prices approximating those prevailing in the United Kingdom consumption would probably have been about 5.5 million tons.

The high consumer prices of beef and veal in the EEC and most other Western European countries is apparently not due to significantly high rates of protection of beef production, except as beef production is a by-product of dairy production. Put another way, if beef production were independent of dairy production in the EEC and other high beef price countries in Western Europe the rate of effective protection would not be very high. In fact, it may be close to zero. In the EEC the differentials between domestic and world prices are at least as high for the grains as for beef and veal. Two studies of the costs of the EEC farm programs to consumers and taxpayers indicate a higher degree of nominal protection for grains than for beef and veal.[16] While it is true that relatively little grain is fed to cattle to produce beef in the EEC, land prices are affected by the prices of grain. With no limitations on the amount of grain that can be produced in the EEC, other than the limitations of profitability, the rent on land used to produce forage must be equal at the margin to what the rent on that land would be if used to produce grain. While much of the land that is used for pasture cannot be used for producing grain, this is not true of large areas used for producing green forage and hay. The recent changes in farm land values are clearly consistent with this interpretation of the effect of high grain prices on land rents and values.

The consequences of the price support policies in most of Western Europe are to discourage the consumption of beef because of high consumer prices and to increase the amount of beef that is available as a byproduct of the dairy industry. However, beef production as a separate enterprise is not being encouraged by the existing price relationships. It is true that the beef-

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[14] Probably an underestimate; based on data in The Atlantic Institute, *A Future for European Agriculture*, The Atlantic Papers, 4, 1970, p. 63.

[15] William P. Roenigk, *Agriculture in the European Community and the United States*, ERS-Foreign 307 (Washington, 1971), pp. 2 and 8. Estimate based on 1969 population and 1966/67 through 1968/69 per capita consumption.

[16] The Atlantic Institute, *op. cit.*, p. 63 and G. R. Kruer and B. Bernston, "Cost of the Common Agricultural Policy to the European Economic Community," Foreign Agricultural Trade of the United States (October, 1969), p. 12. The estimates of nominal protection (1967/68 or 1968) were: Wheat, 68 and 85 percent; Barley, 65 and 42 percent; Beef and veal, 59 and 75 percent.

milk price relationship is relatively high in the EEC — an effort is made to keep it at about 7 to 1 compared to about 5 to 1 in the United States and the United Kingdom. But for a separate beef enterprise the relevant comparison is with feed prices. Here the beef-barley price is 8 to 1 in the EEC compared to 9 to 1 in the UK and more than 12 to 1 in the United States. Thus the farm product with the most rapidly growing demand — beef — is being adversely affected by high consumer prices, on the one hand, and a low rate of profitability, on the other hand.

If the EEC as well as other Western European countries were to lower grain prices to near grain import costs beef production would be affected. It would be possible in this situation to have a significant increase in the amount of grain fed beef in Western Europe. If EEC farmers could purchase feed grains at $60-65 per ton instead of $90-95 per ton, grain feeding to beef would become profitable at beef prices lower than those now prevailing. In any case, if there were free trade in farm products the Pacific countries should not assume that the beef market of Western Europe would be there for the taking. Undoubtedly beef imports would increase from recent levels but there would also be a very significant increase in local production. Such an increase would have to occur if the expanding demand were to be met at prices below those now prevailing in most of Western Europe.

While this paper is primarily concerned with the policies of North America and Western Europe, it is hardly possible to discuss international trade in beef without mentioning Japan. The third factor that has restricted international trade in beef is the policy of the Japanese government. Beef prices are very high and very little beef and veal are imported. It appears that current Japanese agricultural policy is to meet most of its domestic consumption of beef, veal, pork and poultry by protecting livestock production and rapidly expanding imports of feed materials. A different policy could result in a substantial expansion of imports of beef and veal as well as of other meat products. However, it is probable that of the various meat products Japan would have the greatest difficulty in producing beef and veal at prices that were reasonably competitive with potential imports. The famous Kobe Beef would probably survive a substantial expansion of beef imports; since it is unlikely that this type of beef can be produced in large quantities it would only take a very small market to maintain prices at recent levels.

What is at stake is whether there is a substantial market for fed beef of a different type — such as the choice grade in the United States — that could be produced in Japan. The major problem, I suspect, would be to obtain adequate numbers of young beef animals for fattening. The limited geographic area of Japan would mean that reliance would have to be placed upon imported feeder animals. Here distance from the major potential sources of such animals would probably serve as a major barrier to a reasonably low cost operation. However, one can't rule out the possibility of a fleet of B-747's flying from Australia or even North America to Japan loaded with calves weighing 50 to 100 kilograms. At one time there was a fairly significant movement by air of young calves from the United States to Italy.

Japan now has a level of per capita incomes that could support a substantial expansion in the consumption of meat products and especially of beef. While tastes may be a factor in the current low level of meat consumption — about a quarter of Italy's level — the major influence on the level of meat consumption by 1980 will be the price and trade policies followed by the Japanese government. Where it was possible to expand local production, domestic consumption of animal products increased substantially between

1955 and 1967; where domestic production did not increase, domestic consumption stagnated. In 1968 Japan imported $2.4 billion of agricultural products; of this total only $164 million consisted of meats and dairy products; a large fraction of the meat imports consisted of lamb and mutton, products not produced in Japan in significant quantity.

The following data indicate the levels of per capita production and consumption for 1955 and 1967 in Japan of the major animal products:[17]

	1955 (kilograms)	1967
Beef and veal		
Production	1.55	1.60
Consumption	1.1	1.2
Pork		
Production	0.71	5.90
Consumption	0.8	4.6
Poultry meat		
Production	0.37	3.05
Consumption	0.3	2.4
Eggs		
Production	4.04	12.50
Consumption	3.4	10.1
Milk		
Production	11.2	36.0
Consumption (fluid)	6.2	22.5
All meat		
Consumption	3.3	11.1

Per capita beef and veal production and consumption changed hardly at all, while per capita production and consumption of pork each increased five or more times, poultry meat by seven times, and egg and milk production and consumption approximately trebled. In 1967 Japan imported about 13,000 tons of beef and veal or only 0.13 kilograms per capita. If beef consumption per capita had increased at the same rate as pork consumption or to about 6 kilograms per capita and all of the increased consumption had been supplied by imports, beef and veal imports would have been in excess of 500,000 tons in 1967 instead of 13,000 tons. If beef and veal consumption were at the Italian level of about 21 kilograms per capita, total consumption would have been about 2.1 million tons instead of 120,000 tons. There is no particular reason why Japan should have the same composition of meat consumption as Italy, where almost half of the total consumption consists of beef. The only reason for the comparison with Italy is the approximate equality of per capita national incomes and to indicate how large would be the increase in Japan's consumption of beef and veal, relative to the present volume of world trade in beef and veal, if Japanese consumption moved to

[17] OECD, *Agricultural Statistics, 1955-1968* (Paris, 1969). Production and consumption data are not strictly comparable with respect to absolute levels.

the Italian level. It is not meant as a prediction nor as an indication that the Japanese diet should change in this way. But these comparisons do indicate that future developments in Japanese beef consumption could have a major impact on international trade in beef and veal. Whether there is a large expansion in Japanese imports of beef and veal seems to depend primarily upon policy decisions rather than upon demand considerations.

Other Animal Products

The trade and agricultural policies of Western Europe and North America do not seem to have significant adverse effects upon the trade in other animal products that are of interest to the other Pacific countries. The wool policy followed by the United States has little to commend it from a domestic standpoint, but tariff rates were reduced by the full 50 percent in the Kennedy Round and are now at fairly reasonable levels. The use of deficiency payments means that domestic prices to consumers are also at reasonable levels. Wool production is declining in the United States; it fell by almost 40 percent during the 1960s. Imports remained about stable despite the decline in tariffs at the end of the decade. The continued improvement in synthetic substitutes for wool seems to be the main threat to Australian producers, not the wool policies of the United States.

The Pacific countries, other than the United States and Canada, have little interest in pork. In any case, there is little protection of pork production in either the United States and Canada and the effective protection of pork production in the EEC is no more than zero; it may well be negative.

Concluding Comments

It may be noted that most of the adverse effects of U.S. agricultural and trade policies upon international trade in livestock products have been discussed above — the high price supports the dairy products, the deficiency payments on wool, and the mild restraints upon beef and veal imports. The U.S. does not have price supports on any of the animal products other than dairy and wool. Nor are there any direct subsidies for beef, pork or poultry production. During recent years very little use has been made of export subsidies for animal products; occasional and limited subsidies have been paid on poultry meat and our recent concern for the British consumer has resulted in exports of butter assisted by export subsidies. Through the food stamp plan and school lunch program the consumption of various animal products has been increased to a small extent. The output of livestock products may have been reduced to some small degree by the various land retirement or set aside programs that have been in operation. I do not think the effects on output have been substantial, but at least the programs have not encouraged expansion of livestock production.

Except for butter (or butter oil) and dry skim milk only limited quantities of animal products have been disposed of under P.L. 480. In 1969/70 P.L. 480 shipments of animal products amounted to $91 million; of this 90 percent consisted of dairy products.

It is clear that there are substantial barriers to international trade in dairy products and beef and veal that affect the low cost producers in the Pacific area. In the case of dairy products governmental policies in North America and Western Europe expand production and restrict consumption

and thus deal a double edged blow to trade. In the case of beef and veal the high price supports for dairy products induces higher levels of production than would otherwise occur though encouragement of beef production as a separate enterprise does not seem to be of much significance. In fact, in Western Europe high grain prices have limited the possibilities of developing a beef industry relying on grain feeding. However, throughout much of Western Europe high beef prices have resulted in reducing the level of per capita consumption significantly below what might prevail under free trade. It is clear that Japanese policy has substantially reduced beef consumption without resulting in any significant expansion of domestic beef production.

With rather modest changes in the prices and trade policies affecting dairy products in North America and Western Europe and beef and veal in Western Europe and Japan the 1970s could witness a substantial growth in world trade in dairy products and beef and veal. For other animal products the possible expansion of international trade appears to be much more limited.

COMMENTS BY MR. J. E. GANDER

The main conclusion in Dr. Johnson's paper was that the variety of substitution and trade restraining policies in the United States and Western Europe have probably reduced consumption and trade in dairy products and perhaps, to a lesser extent, in meat products. These policies have mainly had an impact on the trade potentials of New Zealand, Denmark and Ireland. However, we cannot expect very rapid changes in these policies as a result of Dr. Johnson's conclusions.

Many considerations other than the traditional demand/supply factors mentioned in the paper affect the production, trade and marketing of these products. Dr. Johnson mentioned the importance of the quality factor, especially in North American consumption regarding fresh and frozen beef. It is also important in regard to fresh and fluid dairy products. The support policies influencing milk production are very important since the level of milk production also sets a floor of availability under other dairy co-products and meat co-products. Imports into the prime consuming areas of North America and Europe will face these quality and support restraints for a long time to come.

Since Dr. Johnson did deal with absolute price/cost comparisons, he might have briefly discussed the transportation and storage cost differentials that significantly affect the movement of these products between countries. Other factors which greatly complicate any comparative, quantitative attempt to analyse the factors affecting production, consumption and trade in these products are regional expansion policies, irrigation programmes, tax policies and differential rates of protection and subsidization on interrelated products.

One of the most significant relationships in the paper arose between feed grains and livestock and poultry. Government policies, which are already directed toward shifting agriculture away from wheat production which has become less attractive in North America into feed grains, may well blossom to cover livestock production and consumption and overlay the already complex programmes.

The impact of large technological changes in other industries or agriculture cannot be ignored. The rapid growth of poultry production in North America mentioned by Dr. Johnson is one aspect of agriculture which has developed assembly line techniques of production, causing prices to fall significantly relative to other meats. The growth of synthetic dairy products and, on the horizon, synthetic meats, in view of the relation between high prices and the gradual disappearance of products like butter and natural fibres, leaves the future indefinite for these products. These matters may force the not unusual situation that our careful economic analysis will be overtaken by other events before it can have any appreciable effect on policy.

Dr. Johnson's price elasticity analysis, which of necessity assumes constant cost conditions, favours increased dairy production in Denmark, Ireland and Oceania, but I wonder whether a substantial increase in supply can be forthcoming, under conditions of constant unit costs, in such restricted areas as Denmark and Ireland. I would expect increasing land and feed costs, perhaps enough to change relationships quite materially, particu-

larly in view of what should become an increasingly attractive industry in other parts of Europe.

There appears to be some absorptive capacity at the intermediate processing levels that takes up any reduction in the basic supply prices by an additional margin in the distributing system. This is a difficult problem and may make the analysis of supply and demand elasticities a little more complex than can be allowed for here.

It is regrettable that the paper did not consider income elasticities of demand for dairy products and meats. As Professor Hay said, in many respects income elasticities, especially in regard to the dynamic Pacific area, as demonstrated by the case of Japan.

The introduction of Dr. Johnson's paper raises one of the most fundamental questions in the economic analysis of agriculture, namely, to what extent must the analysis of prices, costs, productivity and trade invariably be overlaid by the Corn Law and the Sacred Cow approach? Dr. Johnson mentioned the problem many years ago in his first book, for the problem is almost as old as agriculture itself. Agriculture is a sociological phenomenon, a way of life rather than a way of earning a living and this of course gives rise to the income support policies to a very large extent. Therefore we must ask how useful is the micro-economic analysis of agriculture and how much will these other considerations dominate the problems. Perhaps we should turn this around and ask to what degree all the other industries are moving toward the agricultural pattern in which the sociological and political considerations are going to override the purely economic questions.

DISCUSSION OF THE PAPERS

by

SIR J. A. CRAWFORD and PROFESSOR G. H. BOARD
PROFESSOR D. G. JOHNSON, and PROFESSOR K. HEMMI

In reply to Mr. Gander's comments, Professor D. G. Johnson said it was correct that the gap, due to freer trade in dairy products, between expected reductions in production and increases in consumption was unlikely to be met by increased production by the only efficient producers — Denmark, Ireland and New Zealand. He said if there were free trade in dairy products, the level of prices of those products moving in international trade would not be much lower (perhaps 15 to 20 percent) than they now are, except for reductions in feed costs in places like Western Europe since the potential for expansion in low cost areas is not that great. Consequently, much of the protection now imposed is largely not required to maintain what by most standards would be relatively satisfactory prices for dairy products. He said the same is also largely true for beef.

Professor Johnson replied to Mr. Gander that he did not emphasize income elasticities simply because the argument he made was that whatever is demanded should be produced where costs are lowest and this would occur under free or freer trade. Obviously, with regard to the future prospects of a particular commodity, income elasticities are very relevant.

Responding to Professor Hay's comments, Professor Drysdale, who presented Sir Crawford and Professor Board's paper in their absence, commented that the concentration in the early phases of the paper on the farm income problem is due to the paper's emphasis on political strategy more than on economic objectives. He said Sir Crawford would also recognize and take into account the adjustment problems elsewhere. Professor Hay wondered where Australia's comparative advantage really lay, but Professor Drysdale replied the answer was obvious from Professor Grale Johnson's paper and table one on page 18 of Sir Crawford's paper. Nevertheless another participant commented that this table did not include Canada and New Zealand as alternative suppliers and that there is a lot of other evidence of Australia not being a particularly efficient agricultural producer. The rather large drop in agricultural incomes over the past 20 years of 30 to 50 percent was cited as good evidence of this so that more evidence than table one was said to be required to support these statements.

Professor Hay urged Australia to transform its production structure. However, Professor Drysdale pointed out that Australia along with others is in a substantial process of transformation which has caused the problems emphasized in the paper. He said it was rather hypocritical to urge a transformation on Australia without considering the importance of the transformation problem in industrial countries which are importers of agricultural products. He emphasized Sir Crawford's point that to isolate agricultural from manufactured goods trade is a tradition in industrial countries that cannot be supported by Australia and other primary producing

countries if there is to be serious modification of trade barriers in the Pacific area.

Professor D. G. Johnson said that the Australian problem was simply that two of its major export earners — wheat and wool — have a bleak present and an even bleaker future. He did not see any very great hopes for freer trade or even free trade in these products solving any country's problems more than very temporarily. Wool is being displaced by synthetics and wheat, except for some Manitoba No. 1 wheat, must simply become priced as a feed grain given the production capacities around the world and even assuming only modest effects of the 'green revolution'. Professor Johnson said that the gloomy prospects of these two was why Sir Crawford was so energetic about beef and veal since they do have a bright future.

A Japanese participant indicated that Japan would welcome increased exports of primary products from Australia and Canada if they wished and if they would compensate by relaxing barriers to Japanese exports of manufactured goods. This sort of vertically specialized trade is very profitable to both sides, but Australia and Canada always complain about wanting to export more highly manufactured goods. He wondered whether this course is economically feasible or profitable for these countries to pursue.

The participant from Singapore criticized the lopsided approach of all the papers on agriculture in their concentration on the agricultural problems of the rich, industrial nations while completely ignoring the problems of the predominently agricultural nations of Southeast Asia. Most participants generally agreed with this criticism. One Japanese participant suggested Japan ought to give careful consideration to the question of preferential access to agricultural imports from less developed countries which are competitive with those of Australia, Canada and New Zealand. An Australian participant said he also was distressed by the emphasis in Sir Crawford's paper on Australia's rural income problem when incomparably worse poverty problems existed in the world. A wealthy country like Australia could solve its own problems and a first step would be to reduce its tariffs. He noted that Australia, along with Japan and Germany, has had large balance of payments surpluses in the past year with reserves rising by 50 percent from a very satisfactory level. Thus Australia could very easily reduce its tariffs across the board without looking to Japan for help. However, he agreed with Sir Crawford that there was little prospect of rapid, substantial, unilateral or bilateral reductions of tariffs in the next few years although the protectionist climate may be slowly changing.

In response to the Singapore representative's query about Australia's trade policies toward products of Southeast Asia compared to the protectionist policies of the European Economic Community, Japan and the U.S., an Australian participant said that Australia does have a preferential scheme for the exports of these countries. However, Australia accepted the scheme reluctantly and it affects much less than one percent of imports and has very small preferential margins.

The representative from Singapore mentioned the obligation of the advanced countries to assist the development of the poor, primarily agricultural nations. The industrialized countries could do so in one important way by lowering their barriers to agricultural imports from these countries. A major topic of discussion was the fact that this would require more rapid structural change on the part of the developed countries in shifting resources out of their relatively inefficient agricultural sectors. One participant from the U.S.

said that Japan, by maintaining high levels of protection, and the European Community, by structuring world prices by the restitution system mentioned in Sir Crawford's paper, determine policy and price levels for every other country. He said that Japan and the European community must realign their policies if they want liberalization of other's policies and that the less developed countries trade prospects entirely on the decisions of the rich ones in coming to some understanding about realigning their exports. A participant from an international institution emphasized that, while the process of adjustment assistance to agriculture and other industries will be an extremely difficult and central issue in the 1970s and the industrial countries that handle it best will be least strained, it is very dangerous for the developing countries to rest their hopes on such uncertain policies. Of course the developing countries should explore all the markets they can and all nations should be attempting to free more trade, but they ought to explore more carefully the gains from trade with each other.

A Japanese participant outlined the difficulties due to the decline of the agricultural sector in Japan — the excessive outflow of population from rural areas and the low farm incomes. The rapid decline in rural population has been leading to deteriorating public finances and thus public services and a serious distortion in the age composition of the remaining population. The young people move off the farms most easily, leaving behind the older age groups which are not only less productive because of age but also because they contain a relatively large proportion of women. The men often work temporarily or full-time in nearby labour-intensive industries to supplement their incomes, but in remote areas, even this alternative is not available and there the income problem is most serious. Thus, this participant said that while in the long-run Japan should abolish agricultural protectionism to the benefit of both Japan and exporting countries, the problems of moving reluctant peasants and maintaining their incomes while wages in urban areas are rising at 15 to 20 percent a year are very difficult. The difficulties are compounded by the fact that he thought that the agricultural policy of the Ministry of Agriculture is neither articulate nor consistent and is in fact in (a) shambles. He suggested that policies must be devised to allow agriculture to die at a gradual rate.

One U.S. participant observed in regard to the question of changing trade and price policies to move people out of agriculture that in all of the industrial countries the rate of movement of people out of agriculture with no assistance from government has been very rapid since the second world war. Moreover, he has found that, in each of the industrial countries where the date is at all reasonable, the total of non-farm and farm income of farm people has been rising as fast as overall per capita income the past 20 years and their wealth position has been increasing at least more rapidly than that of the working population of their own countries. Consequently, part of the farm problem that governments are trying to solve probably does not really exist and the important thing is the welfare of the farm people regardless of the source of their income.

Another U.S. participant noted that the distortions in the age distribution in rural areas in Japan would tend to disappear in time, but if Japan wants free trade in manufactures, she may not have this time for the rest of the world will press for free trade in agriculture. Then various social welfare policies, such as subsidized retirement, but not price supports, will be needed to speed up the adjustment.

There was some discussion of whether the shift of workers out of agriculture in Japan into light, labour-intensive manufacturing industries would hurt the interests of some manufacturing-oriented developing countries like Hong Kong, Taiwan and South Korea while helping agriculture-oriented ones like Malaysia and Thailand. A Japanese participant thought the conflict of interests would be only partial since the wage rate in Japan, even in rural areas, is three to four times the Hong Kong rate. Another participant mentioned that Japan is concerned to shift labour not only off the farms but also out of labour-intensive industries since its comparative advantage lay in more sophisticated products and even now it is with these products that Japan is having trouble with the U.S., textiles being a passing problem. A U.S. participant pointed out that not more than six or seven million people were left in agriculture on a full-time basis in Japan and of these not more than 1/4 to 1/6 lived in remote communities. Consequently, the problems of age distribution and the shifting of workers out of agriculture do not constitute a significant trade probelm nor affect the competitiveness of Japanese industry, but rather they are an enormous domestic human problem. Unfortunately Japan is trying to solve it just like all the other industrial countries — by propping up farm prices — but higher farm prices do not help these people one bit since the level of their farm output is small.

Finally, summing up, it was said to be vital to distinguish between the agricultural problem and the poverty problem in the adjustment process. Looking at the cash income from agricultural production rather than the income of people classified as rural dwellers gives a misleading picture of the poverty problem. There is a combination of arguments for support prices that reflect two quite different interests. The large efficient farmers want to maximize the value of their land and are claiming an income from society on the basis of an argument referring to poor farmers who in fact get nothing out of support prices. If people are marooned in a poverty pocket, policy should be designed to try and move them out. But it was emphasized that no government is really going to remedy farm poverty in the sense of making farmers as well off as anyone else, for this type of policy only makes them a little better off while perpetuating their poverty.

Development of Processing Industries in Tropical Countries

FACTORS THAT INFLUENCE THE LOCATION OF PROCESSING INDUSTRIES IN TROPICAL COUNTRIES[1]

by

H. VANDENDREISSHE

O.E.C.D.

Introduction

This paper is based on the premise that if the establishment of processing industries is to contribute in any way to the economic development of tropical countries we must consider as processing the whole range of industrial transformation processes undergone by a particular commodity from raw material to end-products. This is justified since commodities exported by LDCs are already subjected to some elementary processing, usually required by technical considerations, and yet their nature as raw materials has not changed. Given the emphasis upon industrialisation this allows us to view the establishment of processing industries as contributing to the vertical diversification of tropical economies and as offering an alternative to other forms and policies of industrialisation.

Among the processed products of interest to tropical countries are the semi-manufactures and manufactures elaborated on the basis of tropical commodities, agricultural foods and raw materials, hides and skins, and timber. Throughout this paper we shall concern ourselves only with these products, to the exclusion of minerals and fuels. All these products have in common a high natural resource content. Consequently, the land factor cannot be ignored in an *a priori* examination of locational considerations affecting the international distribution of processing industries. The question that immediately comes to mind is whether the land factor can be made the basis of trade in processed intermediate or end-products.

What light can economic theory shed on this question? First we will contrast the teachings of locational theory in its international applications with those of trade theory. Then we shall weigh the different elements entering into the cost function, including an analysis of the protective barriers which weaken the pull of international demand.

Location Theory vs Trade Theory

There is much overlapping between location theory and trade theory in their respective attempts to explain the international pattern of production and trade. They both concern themselves with the factors that affect the cost of production i.e. natural resources, capital and labour — and with transportation considerations. Yet they differ in purpose. Location theory seeks to determine the lowest cost producer-country of a particular product while trade theory seeks to determine what products a country should specialise in.[2] The former is interested in comparing absolute costs of

[1] This paper is part of a study being undertaken at the OECD Development Centre on the prospects of increased exports of processed tropical commodities from LDCs and the barriers to their trade.

[2] A noteworthy exception to the usual emphasis of location theory on alternative locational patterns for an industry is Lefeber, L. *Allocation in Space: Production, Transport and Industrial Location*, (1958). His general equilibrium approach embraces the spatial flows of several goods and factors and the locational (transport) problem. By maximising the value of all final goods shipped to different markets, optimal production locations are obtained. The optimal locations and the quantities produced at each location for different sectors are determined by several variables: market prices; the prevailing level

(Cont'd on p. 104)

production while the latter concerns itself with relative costs of producing different goods. In the traditional Ricardian example where Portugal is the lowest cost producer of both cloth and wine, locational theory would tell us that Portugal should produce cloth as well as wine while trade theory advises Portugal to specialise in wine and trade its surplus for English cloth.

To the question of which factors influence the location of processing industries, locational theory can at best tell us the reasons why a tropical country may have an absolute advantage in processed products (relative advantage with respect to other geographical locations), while only trade theory would tell us if it has a relative advantage in the industrial processing of its raw materials rather than in the manufacture of other products.

This distinction is not always respected in the literature, where comparative or relative costs may refer either to one product in two countries or to two products in two countries.

Location theory originally evolved within the analytical framework of the autarkic economy. It makes the basic distinction between "natural-resource oriented" industries and "market oriented" industries. First, the physical characteristics of some products, such as perishability of input or output, or the nature of services associated with them, already determine whether an industry will locate at the raw material source or close to the consuming market. As far as costs are concerned, insofar as within a country differences in factor cost can be assumed away, differential costs of transporting inputs from raw material source to processing unit and of outputs to markets loomed larger as a basic determinant of the location of processing industries. All processes for whose location input-output transport cost differentials were not the determining factor were classified under "locationally foot-loose" industries. For those locationally indifferent industries local factors, such as the sufficient availability of labour, public utilities, services, etc., became all important.

Extending location theory to an international framework, where more than two-thirds of trade between countries is made up of intermediate products, makes us realise how rare are products which are purely resource-oriented or market-oriented. Either we should think of a product at different stages of transformation as different products or think of processes as either resource-oriented, market-oriented, or foot-loose. As examples of purely resource-oriented processes are the elementary processing to which most tropical commodities are subjected. Market-oriented processes are those which for reasons of quality, freshness or fashion, have to be performed in close proximity to the consumer, i.e. processes for which short-distance and market information are determining factors. Most intermediate processes remain fundamentally foot-loose.

Although transport costs have always played a central role in location theory and although they constituted a larger share of total cost in the nineteenth century, the international pattern of production was then more influenced by the unavailability of certain factors of production and complementary inputs in LDCs than by subtle weighings of transport vs factor cost differentials. Since the nineteenth century several factors have

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(Cont'd from p. 103)

of technology; the local factor endowment at each production point; and the parameters of the transport function. In Lefeber's analysis equilibrium locations are determined from a given set of market prices, but it fails to explain the determinants of these prices themselves. In effect, Lefeber's theory is not pure location theory but a Walrasian general equilibrium model modified to take the existence of space into account.

tended to increase the relative importance of processing over transport and other costs: First, improvements in transportation technology have drastically reduced the economic significance of distance and time. As a result the share of transport costs in the value of world trade has been cut in half. Second, as a result of several decades of massive doses of social overhead investment most developing countries are now able to meet the demand for infra-structural services complementary to factors as inputs in the production process. As these services and complementary inputs become widely available individual firms do not have to bear a heavy cost penalty for lack of infrastructure and meaningful international cost comparisons become possible. Third, technological developments are taking place which further reduce the locational pull of either raw material source or market. The development of synthetics as substitutes for natural materials has significantly lessened the pull of natural resource availability on the location of a few industries: e.g. rubber and textiles. Similarly, advanced techniques of packaging, preservation and refrigeration combined with a shift of consumption toward less perishable convenience items has the opposite result of lessening the traditional pull of the market: e.g. as regards processed foods and tropical beverages.[3] Finally; for whole lines of products for which local market information used to be at a premium, the spread and speed of modern communications has had the dual effect of standardising consumer tastes and of weakening the gravitational pull of a particular market on the producer.

The net effect of all these forces is to increase the range of products/processes which can be categorised as locationally foot-loose. And it is the foot-loose industry which is most influenced by processing costs, and particularly by the cost of the factor it uses most. In this respect foot-loose industries must be factor-oriented. Inter-country differentials in factor costs thus become primary determinants of the location of industry. This is the realm of trade theory.

Trade Theory and Natural-Resource Intensive Manufactures

We reviewed the theory with processed agricultural raw materials in mind. It is not always clear whether a theoretical proposition includes or excludes these products. Opinions often differ as to the applicability of a particular theorem to a whole group of products. This seems to be the case with the factor proportions thesis. It warrants detailed exposition even at the cost of repeating some well known propositions.

As we have argued above, trade theory does not concern itself directly with the geographical location of an industry. But its search for an efficient pattern of exchange of goods implies an international division of labour ideally suited to fulfill the conditions of world economic efficiency. If trade theory were able to prescribe which trade pattern would entirely fulfill these conditions it would be a simple matter to check the implied production pattern to see which location is most suited to the establishment of a particular industry. As was demonstrated by Ricardo, a locational decision based on comparative cost grounds will always be superior to one based on absolute advantage.

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[3] Even a product whose quality is as perishable as roasted coffee is now primarily marketed in vacuum-sealed cans. Abstracting from the even greater potential made possible by instant types of coffee, there is now no reason why firms in coffee producing countries cannot compete on equal cost competitive grounds with traditional coffee processors.

Traditional trade theory comes close to such a prescription particularly in the form of the Heckscher-Ohlin thesis. This model assumes two factors (capital and labour), postulates the international identity of production functions, and makes international differences in factor endowment the crucial and sole determinant of comparative advantage. Commodities can then be ranked in terms of the relative factor intensities embodied in their production. The Heckscher-Ohlin thesis states simply that this ranking will correspond with a country's comparatively abundant factor. If we define the relative abundance of a factor in terms of its relative cheapness, this theorem has been shown to be logically valid under the following set of conditions: (a) international identity of production functions, (b) constant returns to scale, and (c) non-reversibility of factor-intensities such as a given commodity is factor x — intensive in relation to another at all relevant factor price ratios.[4]

The Heckscher-Ohlin characterisation of trade has been widely accepted as eminently sensible. Scepticism has been voiced as to its utility however, as a result of two disturbing pieces of evidence. The first concerns Leontieff's startling results when he found that U.S. exports are labour-intensive and its competitive imports capital intensive.[5] The second concerns Minhas' demonstration that far from being a theoretical curiosum, the reversal of factor intensity is an empirical possibility within the range of relevant factor price ratios.[6]

Minhas' results were obtained by ranking U.S. and Japanese industries according to capital intensity. Since the Spearman rank correlation coefficient is significantly different from unity it throws some doubts upon the existence of a direct relationship between factor endowment and trade pattern. It becomes quite possible for a labour (capital) abundant country to export its relatively capital (labour) intensive commodity, and it is not legitimate to deduce a country's relative factor endowment from the relative factor-intensities of exports and import-substitutes.

Minhas' results have since been questioned on the basis of the inclusion in the ranking test of such natural resource intensive industries as agriculture, processed agricultural products and processed foods.[7] Critics contend that the omission of these industries from the rank correlation test would move the Spearman coefficient within the acceptable reach of unity needed to validate the Heckscher-Ohlin theorem.

The phenomenon of reversibility is made possible by differential rates of substitution of capital for labour between industries. This can be illustrated as follows on a logarithmic scale, with capital labour ratios fitted against the ratios of wages to capital costs. It illustrates Minhas' suggestion that inter-industry differences in the parameters of the production function are technically speaking important enough to allow for a cross-over point within the range of observable price ratios. From Minhas' data it would

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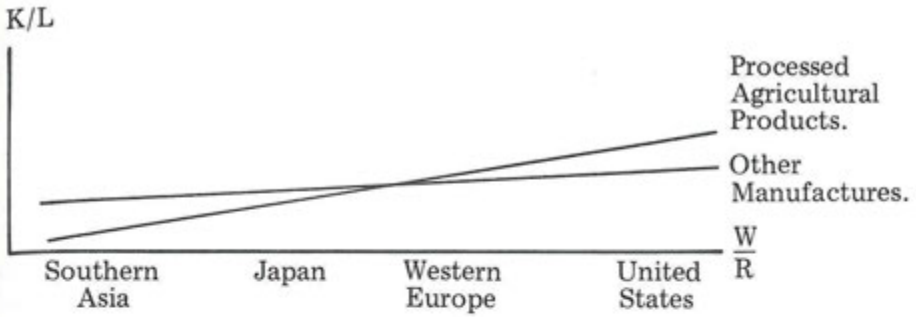
[4] For a survey of the theoretical literature and empirical verifications, cf. Bhagwati, J. "The Pure Theory of International Trade" in *Economic Journal*, March, 1964, P. 1 — 84.

[5] Leontieff, W. "Domestic Production and Foreign Trade: the American Capital Position Re-examined", *Economia Internazionale*, vol. 7, 1954.

[6] Minhas, B. S. "*An Economic Comparison of Factor Cost and Factor Use*; Amsterdam, 1963, chap. 3.

[7] See Hufbauer, G., Appendix on "Factor Intensity-Reversals" in his *Synthetic Materials and the Theory of International Trades*, (Cambridge, Mass., 1966), and Ball, D., "Factor-Intensity Reversal in International Comparisons of Factor Costs and Factor Use", *Journal of Political Economy*, February 1966, quoted in Lary, H. B., *Imports of Manufactures from less Developed Countries*, N.B.E.R. New York 1968, p. 57.

Hypothetical Illustration of Factor Intensity Reversals
(with constant elasticity of capital-labour substitution)



appear that the phenomenon of reversibility is observable in industries which allow a high ratio of indirect to direct capital. Reversibility would then be largely associated with the possibility of substituting indirect capital for labour.[8] Not only does this phenomenon rob the factor proportions theory of any predictive value, but it leads Minhas to the ominous conclusion that "the labour abundant, low wage rate countries would tend to hold comparative advantage in those industries which have low elasticities of substitution between capital and labour *even though* those very industries happen to be relatively capital-intensive at the prevailing cost of labour and capital."[9]

This function is of obvious importance to less developed countries since natural-resource intensive manufactures (excepting minerals and fuels) not only are most liable to the possibility of factor-intensity reversal but also offer the greatest possibilities of substituting labour for indirect capital.

Several attempts have been made to make the Heckscher-Ohlin theorem more predictive by the inclusion of more factors of production: human capital, unskilled/skilled labour, or R and D expenditures on new products. Several new models evolved from these efforts: the human skills account, the technological gap model and the product-cycle theory. These models have been reviewed elsewhere.[10] Suffice it to say that they do not deal specifically with natural-resource intensive manufactures. Their authors would agree with Linder that the classical factor-endowment theory explains the pattern of trade in primary products, but that the land factor cannot be made the basis of trade in manufactures.[11]

As Haitani points out "since necessary raw materials can be imported, the cost advantages or disadvantages of raw materials are usually attributable to transport-cost differences and not to factor endowments."[12]

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[8] Minhas, B. S., *op. cit.*, p. 40.
[9] Minhas, B. S., *op. cit.*, p. 48-9 (his emphasis).
[10] Corden, W. M., *Recent Development in the Theory of International Trade*, Special papers in International Economics No. 7, Princeton, 1965, and Sherk, D. R. "The New International Trade Models and their Relevance for Developing Asia", *The Malayan Economic Review*, Oct. 1969, p. 1-7.
[11] Linder, *An Essay in Trade and Transformation*, Uppsala, 1961, p. 17.
[12] Haitani Kanji, "Low wages, Production Efficiency and Comparative Advantage", *KYKLOS*, 1971, No. 1, p. 78.

And since cost of transport considerations are growing less important, the industrial processing of raw materials, like that of any other intermediate input, is increasingly factor cost oriented.

The new trade models have however introduced several factors which added to the prescriptions of the factor-proportions theory help in identifying the sorts of products in which developing economies might hold a comparative advantage. As Donald Sherk puts it these are "products which are unskilled labour-intensive and possibly fixed capital intensive, which require for their production a relatively standard technology, products whose thresholds for economies of scale are low to moderate, and products which are reasonably undifferentiated ensuring high price elasticity and which require no important servicing facilities. . ."[13]

It would appear that this description would include a good proportion of natural resource intensive products particularly at the semi-manufactured stage, but also at the mass-produced and marketed consumer level.

The Differential Cost Function

Since trade theory does not give us more than a presumption that tropical countries might have a comparative advantage in the processing of locationally foot-loose natural resource intensive industries, we have to examine item by item the different components of their cost function to determine how they fare on absolute cost grounds. If we compare the delivered cost to the consumer from each location — one in the exporting (producing) country, the other in the importing (consuming) country — both functions have five major components to be weighed against one another: the cost of raw material input, the function of processing costs, the cost of transport, the element of fiscal protection, and marketing costs.

Definitions:[14] per unit of output

I — cost of raw material input
C — cost of processing
d — transport cost
P — cost advantage due to fiscal protection
M — marketing costs
t — specific tariff or tax

x — exporting (producing) country
m — importing (consuming) country
r — raw material
p — processed good

In a two-country world of free trade and perfect competition the raw material producing country will have an absolute advantage in processing for export when

$$(1) \qquad I_x + C_x + d_p \leqslant I_m + d_r + C_m$$

After introducing restrictions to trade and competition, equation (1) becomes

$$(2) \qquad I_x + C_x + d_p - P_x + M_x \leqslant I_m + d_r + C_m - P_m + M_m$$

If we balance competitive advantage against competitive disadvantage, processing will be performed in the exporting country when

$$(3) \qquad (I_m - I_x) + (C_m - C_x) \geqslant (d_p - d_r) + (P_m - P_x) + (M_x - M_m)$$

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[13] Sherk, D. R., *op. cit.*, p. 17.
[14] This is a revised and expanded formulation of P. Kilby's model in *Industrialization in an Open Economy: Nigeria 1945 — 1966*, Cambridge, 1969, p. 169.

that is, when an absolute advantage in production costs outweighs the net effect of the different elements of protection shielding already established producers in consuming countries. It pits locational factors of supply against net obstacles in the way of international demand.

On the costs of processing there is little we can add to what was discussed in the previous section. For the manufactures of interest to tropical countries the technological gap factor or the highly skilled labour factor are unimportant except for those products in direct competition with synthetics. For most of these manufactures, especially labor-intensive ones but also the capital intensive ones with a high ratio of unskilled to skilled labor, there is a strong presumption of a potential advantage in favour of tropical countries. With respect to natural raw materials in competition with synthetics it should be pointed out that the competitive edge gained by synthetic products over natural resource intensive manufactures has been made possible by their relative cost ratios as prevailing in advanced high labor cost economies. A valid comparison would use instead the relative costs of producing synthetic products in developed countries and natural material competing products in LDC. It might reveal that the latter could remain competitive for another generation or so.

Although the trend of consumer demand (in high income countries) is undoubtedly turned towards high quality products there remains a vast market for the low priced average quality products in these countries. The relevant variable is the relationship between quality and price. And for most intermediate products, perhaps more important than high quality *per se* is the reliability and constancy of quality standards offered.

Input Costs

An item of cost which is often overlooked in trade literature is the relative cost of inputs. It is often assumed since raw material inputs are traded internationally at world market prices that I_x equals I_m (here on an f.o.b. basis) In fact nothing is less certain, although evidence on this count is hard to come by. We have chosen to include differential input costs in our cost function because any difference between I_x and I_m due to other than fiscal reasons may then be looked upon as reflecting the cost advantage per unit of output which accrues to processors in the raw material producing country. This may be due to spoilage or weight loss during transport (coffee and cocoa), to having local access to a higher quality input (oilseeds in some countries), or to the utilization of hitherto untraded raw materials (broken coffee beans for instance which can be treated without significant product quality loss). Since we have ruled out elementary processes which are already performed in tropical countries, any difference that remains between I_x and I_m will be marginal. But even a marginal difference may be a locational factor of prime importance for some products where input costs are a major proportion of total output costs.

One cannot leave a discussion of differential input costs without raising the question of the role of marketing boards and stabilisation funds. Leaving aside for the moment the fiscal role they play, which in practice is often difficult to separate from the services they provide, to what extent has the short-term emphasis upon increasing foreign exchange receipts effectively discouraged further local processing? Even, or particularly when they succeed at setting a unique and "fair" price for the inputs of foreign and local processors alike, are they not in the process removing a major incen-

tive to vertical integration? Vertical integration and the element of market power associated with it admittedly played a major role in the nineteenth century development of now advanced countries.[15] Since, as we shall argue later, a certain degree of oligopolistic power is manifest among already established market-oriented producers we cannot rule out the significance of a similar but countervailing power in the hands of raw material oriented producers.

Transport Costs

Among the many elements of delivered costs we have transport costs, or the differential costs of transporting the finished product and its raw material input. If the unit cost of shipping the finished product is lower than the cost of its raw material input a net saving will occur in favor of location in the exporting country. As it often happens *ad valorem* freight rates are lower for the processed product than their raw material equivalent, yet not low enough to compensate for the reduction in weight or volume. This means that although $\frac{d_p}{I_x + C_x} < \frac{d_r}{I_m}$, $d_p > d_r$. Since the element of insurance in total transport costs is always *ad valorem* based, the relative difference between the two rates will be smaller than suggested by freight costs alone.[16]

The existence of a discrepancy between d_p and d_r is important in its location effects and, as trade theory has recently pointed out, in its allocation effects as well. It implies that distance constitutes an element of protection: "natural" protection as distinct from fiscal protection. This is the reason that leads us to treat differential transport costs as an integral part of protection, that is as a wedge between the export "push" of cost factors and the import "pull" of international demand.

Whether natural protection will favour one location over another depends upon the nature of the goods at different stages of fabrication and the economics of transport pricing. Natural protection is first felt at the raw material production stage. This stage is relevant to our analysis to the extent that tropical raw materials are in competition with temperate zone substitutes (i.e. oilseeds, timber, sugar, etc). Domestic production of raw materials in developed countries will be protected by the cost of transport of the competing tropical commodity. Beyond the primary stage, when transport costs at each stage of transformation are levied at a constant *ad valorem* rate, natural protection (nominal and effective) will be carried forward along successive processing stages. If transport costs were an increasing function of stage of transformation, natural protection would rise and be increasingly biased against processing in tropical countries. If, as we argued above, transport costs are somewhat less than proportional to value, natural protection will weaken with each successive increase in value added. For products on non-competing tropical commodities a regressive structure of freight rates will be a positive inducement to location in the producing country. Effective natu-

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[15] See Caves, R. E., "The Theory of the International Firm", in *Economica*, February 1971, pp. 10-12.

[16] As Kilby has pointed out, there are two elements of transport savings which accrue to the raw material producing country: a) when the importing country re-exports part of its production after processing to a third country; and b), when import substitution is possible, savings will amount not just to d_p, but to $d_p + d_r$ per unit involved. Cf. Kilby, P., *op. cit.*, p. 169.

ral protection of an intermediate process p_1 in an advanced country (when $dp_1 > d_r$) may even be made ineffective if the finished product P_2 can be shipped at $dp_2 = d_r$ (in dollars and cents). For the products of competing tropical commodities natural protection is always a handicap, although with a regressive freight rate structure this barrier will be relatively easier to overcome at higher levels of transformation.[17]

To the extent that $d_p - d_r$ reflects real transport cost differences the efficiency of world resource allocation will not be impaired. If on the other hand it reflects monopolistic pricing practices of shipping companies not only economic efficiency will be affected but, to the extent that monopolistic profits accrue solely to the importing country, it will entail an additional bias against, and real income loss for, the less developed exporting country.

Fiscal Protection

In their effects on value added transport costs have the same effects as differential tariff rates. In equation (3) above it is the net or combined effect of national fiscal structures in both the importing (P_m) and exporting (P_x) countries which will influence the location of a particular industrial process. P is equal to the total of all taxes (net of subsidies) imposed on the processed product p minus the total of all net taxes on its input r in a particular country; or

$$(4) \qquad P_m - P_x = (t_{pm} - t_{rm}) - (t_{px} - t_{rx})$$

where $(t_{pm} - t_{rm})$ may also include transport costs $(d_p - d_r)$. In this formula it is simpler to think of t as referring to import taxes, either on the product (t_p) or on its input (t_r); but it can and should include the whole series of indirect, excise, production and consumption taxes (positive or negative) which are imposed on p and/or r.

The direction of their net effect on location is obvious. In this formulation any positive effect will favour a market location and would constitute an additional obstacle to processing in the country producing the raw material. Recent trade theory has attempted to measure the size of this obstacle and in studying its implications has derived the concept of effective protection.

The concept of effective protection is of particular importance to our purpose since it is concerned with the vertical relationship between tariffs and other taxes affecting each processing stage from raw material to end-product. The rate of effective protection is the percentage increase in value added per unit in an economic activity which is made possible by the structure of tariffs and taxes relative to a situation that would hold in their absence. If we assume $I_m = I_x$ and define protection in its broadest sense, the simplified equation (3) in terms of world value added C_x becomes

$$(5) \qquad \frac{C_m - C_x}{C_x} \geqslant \frac{P_m - P_x}{C_x}$$

which as an equality yields the net (or combined) rate of effective protection on the value added by a process in one country over the other. As an

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[17] This paragraph and the next draws freely from H. G. Johnson, "The Theory of Effective Protection and Preferences", *Economica*, May 1969, pp. 124-5, Although for our purposes transport costs are here expressed in absolute terms, the analysis is essentially the same.

inequality, if country M's value added is positively protected, it shows that the degree to which the cost of production factors in country X will have to be lower than in M in order to be competitive is an inverse function of value added by the process and not of output value. This is relevant to the products of tropical commodities since value added by processing, particularly at intermediate stages, is often small in proportion to total costs. Empirical research has shown that calculated effective rates of up to 100% due to tariffs alone are not uncommon on the processing of commodities such as groundnuts, crude coconut oil, cocoa, etc.[18] Moreover, if one isolates the value added by labor (L_m or L_x), on the grounds that since capital moves more freely, differences in capital costs will be relatively unimportant, a small nominal rate of protection may allow L_m to be a multiple of L_x without inducing trade.

In addition to its locational effects another aspect brought to light by the concept of effective protection is its allocation effect. Since resources in a country will tend toward a product whose relative cost over other products is lower, in a trading world resources will be attracted to a product whose relative cost minus protection is lower relative to other products than in another country. In this way resources would tend to favor protected industries. Net protection in M will always have a locational bias coupled with a geographical reallocation of resources in its favor (if we assume fixed exchange rates and mobile resources). But it need not alter an economically efficient allocation of resources between products in each country as long as the net protective rate is the same for all products. If on the other hand M's net protection on a product of interest to X is greater than M's net average protection, resources in M will be diverted into it and will weaken further any comparative advantage X might have in this product. Then as a result of protection, not only is it possible for X to have a locational disadvantage in the processing of a product p for which it has an absolute advantage, but, if M's net protection of p over average is greater than X's comparative advantage in p over average, it is possible for X to have a (comparative) locational disadvantage in the processing of p even when it has a comparative advantage in it. That is, structures of effective protection may be such as to reverse the pattern of comparative advantage.

That rates of protection in developing countries on products of interest to developing countries are higher than average is well known. The following table originally computed by Balassa shows nominal as well as effective rates of protection in developed countries, comparing pre-Kennedy with post-Kennedy Round rates.

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[18] See Harry G. Johnson, "The Theory of Tariff Structure with Special Reference to World Trade and Development" in Johnson, H. G. and Kenen, P. B., *Trade and Development*, Geneva: Droz, 1965; also his *Economic Policies toward Less Developed Countries*, Washington: Brookings, 1966, p. 91 (Table 2); UNCTAD, *Tariff Structures of Selected Developed Countries and Their Effect on Exports of Processed Goods from Developing Countries*, Document TD/B/C.2/9, 17 February 1966, p. 4-6 (mimeo).

TABLE 1

Nominal and Effective Rates of Protection of Manufactures in Developed Countries:
(a) Before Kennedy-Round (b) After Kennedy Round

	U.S.A.		U.K.		EEC		Japan		All Industrial Countries	
	(a)	(b)	(a)	(b)	(a)	(b)	(a)	(b)	(a)	(b)
on All imports of Manufactures										
Nominal tariff	11.5	6.8	15.2	9.1	11.0	6.6	16.1	9.4	10.9	6.5
Effective tariff	20.0	11.6	27.8	16.0	18.6	11.1	29.5	16.4	19.2	11.1
on Imports of LDC Manufactures										
Nominal	17.9	12.4	19.5	14.1	14.3	9.4	18.0	11.7	17.1	11.8
Effective	35.4	23.9	37.3	27.6	27.7	16.9	36.7	20.2	33.4	22.6

Source: Balassa, B. "The Effects of the Kennedy Round on the exports of processed goods from developing areas", UNCTAD, TD/69 Feb. 1968 p. 8.

It can also be deduced from these figures that tariff reductions brought about by Kennedy negotiations are proportionately lower on products of interest to LDCs than on more advanced manufactures. Thus, distortions in the allocation of world resources between categories of products might have increased rather than decreased as a result of these negotiations. The fact that so many processed commodities in BTN 0-24 were excluded from the present scheme of generalised preferences may reinforce this process even further if and when it is ever fully implemented.

To return to the concept of net effective protection of a product, it is useful to illustrate what it means to the parties concerned with a hypothetical example. It is also more realistic to think of a product both as an importable and an exportable. Up to this point we have been concerned with a one faceted processed product: an exportable from the viewpoint of X is an importable for M. If we assume the existence of a domestic market for the processed product in X, the same product will also be an importable for X and an exportable for M. They should be distinguished analytically since within one and the same country a given tax structure will effectively protect an exportable differently from the same but importable product. Short of dealing with elasticities, it is also necessary to introduce certain assumptions about price behaviour and competition. We assume M and X trading exclusively with one another. The World is there on the sidelines only as a reference point to show the costs of inputs and factors without restrictions: We assume $I_x = 200$ and world value added $C_x = 100$ or one third of total cost.

We set out to calculate maximum protected value added in M and X for the product supplying M's market (C_m' and C_x') and, on the assumption that the supplier in M is originally the price setter in X's market, protected value added in both countries for the same product importable in X (C_m'' and C_x''). The schedule of tariffs and taxes is given at the top of Table 2, with specific import duties on the raw material and end-product in M being $t_{rm} = 20$ and $t_{pm} = 70$. The only tax imposed by X is an export tax on the raw material input of which X is the only supplier. Since an export tax is analytically the same as an import subsidy, $t_{rx} = -40$ (and $t_{px} = 0$).

Looking first at our processed product in M's market, the effective protection of X's exportable to M will be determined by differential taxation of processed export (column 5) and raw material export (col. 4). The rate of protection of value added of X's exportable will be

$$P_x' = \frac{t_{px} - t_{rx}}{C_x} = \frac{0 - (-40)}{100} = 40\% \text{ or also } \frac{C_x' - C_x.}{C_x}$$ [19]

Similarly protection of M's importable will be determined by differential domestic taxation of processed import and raw material input (cols. 1 and 2):

$$P_m' = \frac{t_{pm} - t_{rm}}{C_x} = \frac{70-20}{100} = 50\% = \frac{C_m' - C_x.}{C_x}$$

Net protection of M's domestic market is $P_m' - P_x' = 10\% = \frac{C_m' - C_x.}{C_x}$

[19] In terms of P_x in absolute terms per unit of output the effective rate of protection is, more accurately, P_x' / C_x, but since C_x was arbitrarily chosen to equal 100, P_x' and P_x'' are here rates of effective protection. One prime in X refers to an exportable and two primes to an importable; vice-versa for M.

TABLE 2

Hypothetical Example of Effective Protection

Country M						Country X						World Market Prices (7)
Importable (1)		Importable (2)		Exportable (3)		Exportable (4)		Exportable (5)		Importable (6)		
Raw Material Import for Domestic Processing		Processed Import from X		Processing for Export to X		Raw Material Export		Processing for Export to M		Domestic Processing		
Schedule of tariffs/taxes												
t_{rm} = 20		t_{pm} = 70				t_{rx} = -40		t_{px} = 0				
PART A — M price setter in M and X												
						I_x	200	I_x	200			I_x 200
						t_{rx}	40					C_x 100
I_m'	240			I_m'	240	I_m'	240			I_m'	240	300
t_{rm}	20			t_{rm}	20			C_x'	140	t_{rx}	-40	
	260	c.i.f.	340		260			f.o.b.	340	I_x	200	
C_m'	150	t_{pm}	70	C_m''	150					C_x''	210	
	410		410	f.o.b.	410						410	
	P_m' = 50%			P_m'' =	50%		P_x' = 40%				P_x'' = 110%	
PART B — M price setter in M and X price setter in X												
				I_m'	240							
				t_{rm}	20							
					260							
				C_m''	80							
					340					I_x	200	
										C_x''	140	
											340	
				P_m'' =	-20%					P_x'' =	40%	

This means that even if the supplier in X chose an aggressive cost and price cutting export policy with $C_x = C_x = 100$, M's domestic producer could match any reduction in price and get factor returns at least 10% above his rival.

We switch to X's domestic market for the product. We assume that it was originally supplied solely by imports from M at the same price ruling in M. Because of its monopoly position $C_m'' = C_m = 150$. If however X embarks on import substitution, it might be able to supply a small proportion of its domestic market at the price set by M of 410. In so doing X's value added per unit of output sold locally could reach as high as $C_x'' = 210$, an effective rate of 110%.[20] If as is more realistic, X's import substitution drive can only be achieved by undercutting imports from M as assumed in Part B of Table 2, X may lower its local price to 340 with the same effective protection as for exportables ($P_x'' = 40\%$) and drive M's product out of X's market. X's strong market position domestically is due to M's vulnerability. The same import tax structure which protects M's domestic market by 50 per cent, yields a negative protection rate on M's exports of 20 per cent

($P_m'' = \frac{0 - 20}{100} = -20\%$). Net protection of X's domestic market is thus equal to $P_x'' - P_m'' = 40 - (-20) = 60\%$. For the given tax structure C_x'' may always be up to 60% (of C_x) above C_m'' irrespective of output price. Another consequence of treating importables and exportables differently is that the average rate of protection of a product in a country as measured by gross domestic value added by the industry minus the same value added at world prices will be an average of the rates of effective protection of importables and exportables weighed by their respective shares in total output.

Marketing Costs

The possible extensions of this type of analysis are innumerable. Any freight rate, import duty or other internal tax differential which makes $t_p > t_r$ will effectively protect an importable. Any t_r that is not refunded or compensated by a subsidy on the processed export will amount to negative protection of the same product when viewed as an exportable. If we introduce differential marketing costs as provided for in equation (3), any $M_x > M_m$ per unit of output may be interpreted as providing protection of an importable in M. This is justifiable if these costs include the effects of industrial organisation as is warranted in the case of processed tropical commodities because of the highly organised nature of the industry.

It is a characteristic of old established firms that they wield considerable oligopolistic power. The industry is often dominated by a few sellers, where market competition emphasizes product differentiation by means of expensive advertising campaigns. Prices are administered and include

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[20] where $\frac{C_x'' - C_x}{C_x}$ is also equal to $\frac{C_x'' - C_m''}{C_x} + \frac{C_m'' - C_x}{C_x}$

An interesting remark can be made in this respect. The high potential protection of value added on import substitution in X, particularly when it is in part due to the price setting power of the dominant M supplier, shows the fallacies and dangers involved in basing an investment decision on the cost competitiveness of an import substitute with the c.i.f. price of imports. This is just one manifestation of the fact that protection of an importable fosters a high cost structure which discourages exportables.

an oligopolistic profit proportional to the costs of entry. These costs of entry measure the degree of protection afforded already established producers by the prevailing market organisation.[21]

As a variable in our cost function, $M_x - M_m$ would thus include: a) distribution costs, which are likely to be the same for each supplier; b) the special costs or benefits associated with distance or proximity to market, such as information, communications, inland transportation, etc., which will tend to make $M_x > M_m$; and c) M_x will be inflated by the special advertising costs of introducing X's product on market M and by the potential costs of a price war initiated by established producers to drive the new entrant out.[22]

For completeness we can further assume the possibility of import substitution in X. The existence of a domestic market in X for the product is often emphasized by theory and policy alike as a pre-requisite to the establishment of a processing industry. The essence of the argument rests on the importance of economies of scale and efficient size of the production unit to render unit costs competitive. This point undoubtedly shall never be too emphasized. It cannot be separated however from its sequel, namely, that once installed, an optimally scaled plant must be kept operating efficiently at high rates of capacity utilisation.[23] Only a highly motivated and capable managerial staff bent on overcoming one and every obstacle can fulfill this condition. Once this admittedly intangible factor is assumed, the size of the domestic market ceases to be a constraint and it becomes feasible to envisage the establishment of a primarily export-based industrial complex.

Having effectively disposed of the domestic market constraint *qua* pre-requisite for an optimum production unit, we reintroduce it as a strategic factor of prime importance. If we think of a domestic market as an insurance against the possible loss of export markets, the larger the size of the domestic market relative to optimal plant size the lower the potential costs M_x associated with fighting already established competitors on M's market (under c) above).[24]

The net result of all these considerations on marketing costs will still undoubtedly favour producers in M. Then $M_x - M_m$ is likely to be positive and constitute an additional obstacle to the export of processed products from tropical countries. Any differences $M_x - M_m$ will indeed accrue to processors in M in the form of higher factor returns, so that it is

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[21] See Caves, R. E., "Theory of the International Firm", in *Economica*, February 1971, and Bain, J. S., *Barriers to New Competition*, Mass., 1956.

[22] An UNCTAD-GATT document records such an experience: "Very cheap soluble Brazilian coffee appeared in the Netherlands around mid-1967. It was 60% cheaper than Dutch spray-dried soluble coffee. This gave rise to a veritable price war. ... For some months this coffee met with great success, but the two large companies . . . were able to re-establish their positions on the market through a heavy advertising campaign" see International Trade Center, *Industrial Coffee on Twenty-one European Markets*, Geneva, 1969 p. 75.

[23] Witness the vast literature of international organisations on the underutilisation of existing capacity; see also Kilby, P., *op. cit.*, chapter on the difficulties of the oilseed crushing industry in Nigeria. For a review of planning failures due to inattention to marketing, see Abbott, J. C., "Marketing Issues in Agricultural Development Planning", in *Markets and Marketing in Developing Economies*, edited by Moyer, R., and Hollander, S. C., Irwin, 1968; and Mittendorf, H. J. "Marketing Aspects in Planning Agricultural Processing Enterprises in Developing Economies", *Monthly Bulletin of Agricultural Economics and Statistics*, Rome, FAO, 17(4), 1968.

[24] More than a passing reference should be made to the importance of a local market for by-products although in the processing of raw materials it is not always easy to distinguish a product from a by-product. In any case they cannot be overlooked.

fully justified to view it in terms of M's value added and treat it as a form of market protection.[25]

Conclusion

We have sought to spell out the different forces at work influencing the international location of processing industries. Recent trends in the exports of semi-manufactures and manufactures from LDC's have shown the preponderant place occupied by natural resource intensive products within these exports. This was achieved in spite of a structure of protection in developed countries biased against these products. If one takes into account the overvaluation of currencies in LDC's, it is doubtful that on a net basis this bias would be reversed. Actual trade data can then be taken to reveal potential comparative advantage.

There need not be agreement on this theoretical point to see the desirability of redressing imbalances which warp the allocation of world resources. In view of the potential effects of the impending generalised scheme of preferences, the primary concern of the international community in the seventies should go to lowering the remaining duties on the processed and semi-processed products which have been excluded from the scheme.

Short of a major tariff-cutting conference, our analysis shows that there is a lot that individual countries, or a regional association, bent on action, can do. Policies may be initiated, or pressures be brought to bear, on almost every item of the cost function we identified. But the first stumbling block is our relative ignorance of the magnitude of the differential costs involved. Action oriented research covering specific export products or industries can best be undertaken within a regional framework since a locational decision is always based on the net effect of (at least) two opposing cost and protective structures.

On the cost side it was argued that differential input costs and the effect of institutional arrangements on them should not be overlooked.

On the protective side greater acceptance should be granted to export subsidies in LDCs to compensate for the effect of all types of protective barriers shielding already established producers in advanced countries.[26] Such subsidies would be more readily tolerated if we had full knowledge of the extent to which protection already exists. Regional arrangements could also be devised to reduce the extent of differential transport costs particularly when these are due to arbitrary freight rate structures. The cost of transporting the finished product may be at least initially brought down closer to its social cost. The costs of entry into a new market could be drastically reduced with the cooperation of the importing country, and insurance might be provided against price wars.

An industrialisation policy based at least in part on the establishment of highly integrated processing industries from raw materials through each successive stage of fabrication to the profitable end-products would greatly hasten the development of local markets and provide an essential link between the agricultural and industrial sectors.

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[25] At first, the oligopolistic profit accrues to capital, but later, as Galbraith has argued, labour demands its share. The resulting rise in its cost structure would seem to make the industry more vulnerable to outsiders; in fact, it fosters even more powerful protectionistic vested interests.

[26] See Streeten, P., "The Case for Export Subsidies", in *Journal of Development Studies*, July 1969.

COMMENTS BY PROFESSOR A. E. SAFARIAN

Professor Safarian was somewhat critical because of the way in which the paper handled the five functions or types of cost separately. This may have been necessary for purposes of exposition but analytically problems arise not of the interdependence of the five functions.

A major aspect of the marketing costs function is the cost of entry to an oligopolistic industry at an international level. A related question, which is not given enough emphasis here, is the degree to which the large firms are internationally fully integrated. If there is a large, multinational firm that is importing raw material products into its home market, and if it is assumed that the international market for the product is not growing, then if there is a degree of oligopoly in the competing industry in the importing country and if there is a degree of fiscal or tariff protection which permits the large firms to operate as oligopolists, then treating fiscal protection in one function and market entry in another seems to underestimate the importance of the market entry question. It is underestimated to the extent that protection permits oligopolistic practices or to the extent that oligopolistic power is used to increase or maintain fiscal protection. The policy implication is that whatever is done in one of these areas, such as reducing the degree of fiscal protection, will have a compound effect on the other terms.

Professor Safarian thought that research and development expenditures ought to be included in the cost function because in some respects they are a more critical input than some of the others. Research and development activities are deeply involved in Vernon's product cycle theory which might be regarded as an extension of the Heckscher-Ohlin *theorem*. Professor Safarian suggested that, while research and development expenditures were left out of the cost function because they are related to new goods, they ought to be included because of their importance and although this would not result in a product cycle theory it would have important implications for the location of processing industry which produces relatively undifferentiated products.

TRADE IN PROCESSED AGRICULTURAL PRODUCTS, WITH SPECIAL REFERENCE TO SUGAR

by

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This paper contains three parts. In the first, the general question of exporting processed agricultural products from the less developed countries is considered. Recent trends in exports and prices of raw and refined sugar are described in the second while in the third a rather shorter look is given to three other raw and processed agricultural products exported by tropical Pacific Region countries: timber, coconut and oil palm.

1. General

In considering processed products, one encounters a problem of definition: what is the activity "processing"? An F.A.O. paper identifies it as occurring "at an early stage of transformation, following 'handling' and preceding 'manufacture'", but states that "even early transformation stages are regarded as manufacture rather than processing if capital-intensive methods are employed and if much value is added to the primary product."[1] A satisfactory definition is elusive, but I would prefer a concept that does not depend on capital intensity. Perhaps "an early stage of transformation" is sufficient for present purposes — I shall regard sawing logs, pulping timber, or refining sugar as "processing", but the making of furniture, books or confectionery as "manufacturing", even if the former are more capital-intensive than the latter.

"Processing" frequently is thought of as a natural development for an agricultural economy, which, starting from a situation in which it exports agricultural products in a raw state, with the passing of time commences processing activities at home and then exports the processed product. The man in the street may argue "if we can export wool then why can't we export cloth"? The economist thinks "comparative advantage" and reflects that there is further support for the statement that the social sciences contain at least one proposition that is both true and non-trivial.[2] Such a pattern of developing comparative advantage, from raw material and into the processed product, could emerge in an economy, at an early stage of development, if the rate of capital accumulation (physical and human), per man, exceeds that in the importing countries, and if the early stages of processing are more labour intensive than alternative forms of development.

But, of course, there are a number of barriers to such a pattern of development. These barriers may be to the *establishment* of processing activities in the countries concerned, or to *exports* of the processed products from these countries. However the two categories of barriers are not entirely

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[1] F.A.O., "Trade in Agricultural Commodities in the United Nations Development Decade; Part III, Trade in Processed Agricultural Commodities" in *Proceedings of UNCTAD, 1964*, Vol. IV, p. 155.

[2] Paul A. Samuelson, "Presidential Address: The Way of An Economist", in Paul A. Samuelson (ed.), *International Economic Relations*, (Macmillan, London, 1969), p. 9.

separable — for example, if there are economies of scale then barriers to exporting may prevent establishment of production within the country.

Much of the logic behind the idea "if we can export wool, why not cloth" relates to transport costs, and for many products the logic is correct. Thus raw (cane) sugar milling is always located near cane growing for transport reasons associated with both loss of weight and deterioration of the sugar content of cane after cutting. But while transport costs favour the location of many processing activities close to the raw material production, this is not universal. An example of an exception is in tea, where to secure the required blends, packing generally is undertaken near the market: in general, transport routes are such that it is cheaper to carry the different types to the major markets and blend there, rather than to blend at one, or many, of the sources of supply.

In examining the barriers to production and exports of processed products, the question arises as to whether early stages of processing are, in fact, relatively labour intensive. Hal Lary's method[3] of assessing labour intensity is useful for this purpose. His measure is the simple one of value added per employee, the intention being to catch the contribution of human and physical capital in one measure. By dividing value added per employee into two components— wages and salaries, and other — he also obtains measures of the contribution of human capital and physical capital for various industries. Lary found a marked similarity in the rankings of industries by value added per employee across countries suggesting, *inter alia*, that factor intensity reversal is relatively unimportant, at least at the level of aggregation at which he was working. Thus statistics ranking factor intensity in a country for which statistics are readily available and of good quality, may shed light on relative factor intensities for countries for which data do not meet the same standards.

Table 1 gives indexes of value added, and its components, per employee for the United States for a number of activities that may be regarded as "processing". Table 2 sets out similar data for Australia, though with fewer classes of industry. In general it may be seen that processing activities vary widely in regard to the measures of "capital intensity", in relation to human, physical and total capital. Thus processing activities in general cannot be regarded as labour-intensive. Processing of fibres into yarns, of timber and leather may be regarded as labour intensive while cereal preparations, animal feeds, sugar refining and production of vegetable and animal oils are capital intensive. In general, the high capital intensities relate more to physical than to human capital.

Thus not all processing activities may be regarded as being suitable for the factor endowments of the countries producing the raw products. (The same point was made, though on the basis of different data, in the F.A.O. paper submitted to UNCTAD I[4]). Of course if factors of production are mobile internationally, inappropriate factor endowments may not be so much of a barrier. The international corporation with industry-specific capital may locate processing where it is cheapest — and to some extent this will be where labour is cheapest. Thus high *physical* capital intensity may not be a barrier to location of processing in an agricultural exporting country though, of course, in such an industry there may be little benefit to the host country

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[3] Hal B. Lary, *Imports of Manufactures from Less Developed Countries*, (N.B.E.R., New York, 1968).
[4] F.A.O., *op. cit.*, pp. 190-194.

apart from taxation — employment created will be low and remittances abroad high. High *human* capital intensity is more likely to be a barrier, however, as physical capital probably is more mobile than human capital.

It is generally accepted that tariff barriers in importing countries have tended to discriminate against processed goods and in favour of raw materials. Balassa has presented considerable evidence to support this view and that this discrimination will continue even after the Kennedy-Round reductions in tariffs have been implemented fully.[5] Some of his evidence is reproduced in Table 3. The almost universal pattern is that the tariff on the first stage of processing exceeds the tariff on the raw product, so that the effective rate of protection on the processing *activity* exceeds the nominal tariff on the processed product.[6] In general, the tariff escalation is continued through the stages of processing. Balassa also finds "a negative correlation between the degree of protection of processed goods and the relative share of these [i.e. processed] products in imports from developing countries". Japan, with "by far the highest effective duties on processed goods ... imports the smallest proportion of primary products in processed form".[7]

Additional information relating to tariffs on other products is provided in Table 4. Apparent here is the fine selectivity of tariffs in protecting processing and even packing — e.g. tariffs on silk and cotton yarns prepared for retail sale in the E.E.C. exceed those of the same yarns not prepared for retail sale, while tea in retail-sized packs bears a higher duty than tea which is not in such packs.

As has been emphasized in recent years — in part as a consequence of reductions in tariffs — there are important barriers to trade of a non-tariff nature.[8] Whether these discriminate against processed products relative to non-processed is not immediately clear: one example where such a barrier does so discriminate is in coconut oil imports to the U.S. Duty-free imports of coconut oil from the Philippines and U.S. Pacific Trust Territories are limited by quota whereas duty-free imports of copra from the same source are not subject to quota. On the other hand several countries prohibit imports of unprocessed meat from countries in which foot and mouth disease is prevalent but permit imports of canned meat from the same countries. Baldwin's calculations[9] suggest that non-tariff barriers in the U.S. and U.K. impinge with greater severity on imports of primary products than on imports of intermediate and consumer goods or capital goods,[10] but his study is rather too aggregated for present purposes. Walter[11] presents evidence that suggests the non-tariff barriers discriminate against the exports of the developing countries. In commenting on Walter's paper, Baldwin provides an argument that non-tariff barriers do discriminate against the establishment of manufacturing (and processing) exports from developing countries: "Exporters who

[5] Bela Balassa, "The Structure of Protection in Industrial Countries and its Effects on the Exports of Processed Goods from Developing Countries" (Paper prepared at the World Bank for UNCTAD II, 1968).

[6] On a more aggregated basis Baldwin, who takes account of non-tariff as well as tariff barriers, supports Balassa's results for the U.S. (at least when non-traded imports are treated in Balassa's manner) but not for the U.K. (Robert E. Baldwin, *Non-Tariff Distortions of International Trade* (Brookings and Allen and Unwin, 1971), Chapter 7).

[7] Balassa, *op. cit.*, Chapter II, paras. 27 and 29.

[8] In particular see Baldwin, *op. cit.* and Ingo Walter, "Non-Tariff Barriers and the Export Performance of Developing Economies", *American Economic Review, Papers and Proceedings*, May 1971, pp. 195-205.

[9] Baldwin, *op. cit.*, Tables 5 and 7.

[10] An exception is capital goods in the U.K. in 1954.

[11] *Op. cit.*

wish to sell their products in markets protected by non-tariff barriers generally are forced to incur considerably greater cost outlays in finding out what the exact nature of the barriers are than if the protection takes the form of tariffs. Because of the rather significant scale economies associated with obtaining information, this means that new and small exporters of manufactures — like most developing countries — are placed at a substantial disadvantage relative to large established producers".[12]

Another barrier to exporting processed products arises through disequilibrium rates of exchanges supported by import duties etc. in agricultural exporting countries. In such a situation, of course, the return to exporters is less than it "should" be and the cost of imported inputs is greater than it "should" be, because the average import duty etc. must exceed the "devaluation equivalent" effect on the price of imports. Even supposing that exporters can secure refunds of import duty paid on inputs into exports, the disequilibrium exchange rate may still discourage a progression from exporting the raw material to exporting the processed product: the changing comparative advantage will take longer to "reveal itself" when the return on exported value added is maintained below its optimum level by an inappropriate rate of exchange.

Finally there are barriers to exporting processed products which are related to information — the costs of obtaining it and the ability to respond to it. These include "the uncertainties, high costs and long time periods associated with the international movements of goods, ... the ignorance of entrepreneurs in the less-advanced areas regarding the market conditions for manufactured products abroad; and the reciprocal ignorance of entrepreneurs in the advanced countries of conditions in little-known and distant areas overseas".[13] Such barriers are not likely to be so important in the early stages of processing as in the later. And, of course, the more a country tailors its products to suit a particular export market and invests in the provision of information from that market, the greater the loss it will incur if that market disappears. As Vernon points out, the possibility of greater gain may not compensate for this risk of loss: "the entrepreneur who decides that he is unwilling to risk the game of Russian roulette that may be involved in investing in the penetration of a large and potentially profitable export market may be making a rational decision after all".[14] Private and social interest probably diverge here: thus some sort of risk-pooling by several potential exporters, either voluntarily or through a government scheme, may be appropriate. Vernon considers some schemes of this nature as well as policies that may be adopted to overcome other barriers arising from lack of information etc.

Greater awareness in developed countries of the external diseconomies associated with some processing activities may be a factor inducing the relocation of processing activities from importing to exporting countries. Whether this is good for the exporting countries or not is another matter. One can argue that the marginal external cost of certain activities is an increasing function of the size of the industrial centres — e.g. external costs arising from production of smoke. So there may be cases where shifting an

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[12] Robert E. Baldwin, "Discussion", *American Economic Review, Papers and Proceedings*, May 1971, p. 210.
[13] Raymond Vernon, "Problems and Prospects in the Export of Manufactured Goods from the Less-Developed Countries", in *Proceedings of UNCTAD 1964*, Vol. IV, p. 201.
[14] *Ibid.*, p. 204.

activity from an industrial centre to a non-industrial (in this case an international shift) may be beneficial to both. A concrete example of a likely shift due to pollution is in wool scouring. It has been reported that pressures have come from Japan for scouring to be located in Australia because of the pollution caused by the chemicals employed. (I am not suggesting that the shift would be beneficial to the exporting country in this case.)

2. Sugar

The world sugar industry provides examples of barriers to trade in two processed products — raw and refined sugar. Sugar can be produced from a variety of plants, but in particular from sugar cane and sugar beet. There are few countries of the world in which neither is grown, while some countries grow both. The world sugar industry is rather unique in that there is direct competition between a tropical and a temperate zone agricultural product.

Little, if any, international trade occurs in sugar beet or sugar cane, for in both products the sugar forms a small proportion of the weight of the harvested crop, and in both cases the sugar content declines if the sugar is not extracted soon after harvesting. Thus there is a strong transport factor favouring the location of the first stage of processing close to the growing of beet and cane.

Cane sugar passes through two distinct phases of processing — extraction of raw sugar from cane, and the refining of the raw sugar. In the second process sugar generally loses about eight per cent of its weight, but much of this loss comprises saleable by-products. While the processing of beet sugar can also be stopped at the raw stage, it is more common for beet to pass through a continuous transformation to be refined product.[15] As may be deduced from the geographical distribution of exports of raw and refined (Table 5), relatively little cane sugar is exported from the growing countries in a refined state, while little beet sugar is exported raw.

It has been indicated already that cane sugar refining, in terms of its factor requirements, probably is not a particularly suitable processing activity for the less developed countries (see Table 1). Partly for this reason, refining during the colonial period was located in the developed rather than the less developed countries. Additionally, there was an advantage in locating refining near major markets — at the junction of trade routes — so that various sources of supply could support refining on a large scale throughout the year. However even if cane sugar producers — despite their factor endowments — wished to export refined sugar, imports of refined by the major markets are now so heavily restricted that there would be very little return from the refining activity.

Average prices on world "free"[16] markets are shown in Table 6. Two points may be noted:

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[15] In the U.K. in 1963, there were eighteen beet sugar factories, fourteen of which produced white sugar and four (all more than thirty years old) produced raw sugar. In addition there were nine sugar refineries. (International Sugar Council, *The World Sugar Economy: Structure and Policies* (London, 1963) Vol. I, p. 84).

[16] The "free" or open market embraces less than half of total international trade — the balance is sold under preferential trading arrangements, in particular under the United States Sugar Act, the British Commonwealth Sugar Agreement and within the Communist Bloc (including Cuba).

(i) The small difference between the prices paid for raw and refined sugar sold on the open market. The margin for refining cane sugar in many developed countries (including loss of weight allowance) appears to be around 1½-2 cents/lb.[17] The last two columns indicate that there has been little incentive to exporters to refine sugar for export to the open world market: in the years shown the average raw/refined margin did not exceed 1.1 c/lb. and was as low as 0.5 c/lb. This lack of incentive is further indicated by a comparison of the International Sugar Council daily price (f.o.b. Caribbean) for raw sugar and the spot price (f.o.b. European ports) quoted for refined sugar by the Paris sugar market over a period of two years during 1964-1966. The refined price was at all times higher, but never by more than about 1¼ c/lb., and more generally by about ¾ c/lb.[18] The latter figure would barely cover transport across the Atlantic and loss of weight in refining. On occasions refined sugar has in fact sold for less on the world market than the then current price of raw — a real case of negative value added at world prices.

(ii) The variation in the average annual price paid for refined is very little different from that of raw over the period. Thus moving into refined would not provide much of an escape from price variation. Additionally, as import demand for refined probably is more price-inelastic than for raw, any price stability achieved (and this in itself is very doubtful) would be bought at a high cost.

The high protection of the refining activity[19] in developed countries is not, in the main, directed at cane exporters. Rather it is aimed at protecting the domestic beet farmers, factories and cane sugar refineries against exports of refined from other developed countries. Ubiquitous subsidization of production has generated (in years when harvests do not fail) ubiquitous exportable surpluses.

Thus under the present structure of the world sugar market, there is little purpose in sugar exporting countries of the Pacific Region moving out of raw and into refined for the world market.[20] Nor is there any pay-off from moving into refined from the protected markets under the British Commonwealth Sugar Agreement (Fiji and Australia) or the United States Sugar Act (Philippines, Mexico, Peru, Fiji, Mexico, China (Taiwan), Colombia and Australia), for both of these preferential arrangements apply to raw sugar. In relation to the United States Act, (which is to be renewed this year) Professor Donald Horton says: "The former Cuban 'white sugar' quota was not distributed to other suppliers when the Act was amended in 1962. This was a concession to the domestic sugar refiners who depended mainly on foreign raw sugar. Department of State representatives objected strongly to this and urged that a white sugar component of the foreign quota be available to be allocated to countries interested in and capable of developing a sugar refining industry, but their view was not accepted by the White House. A concensus within the domestic sugar industry ... took precedence over

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[17] This is calculated from data contained in *International Sugar Council, op. cit.*

[18] M. G. W. Hallmans and A. S. Ivanov, *A Review of Recent Developments in the World Sugar Market, 1960-65* (International Sugar Council, London, June 1966; mimeo.), pp. 58 and 61.

[19] Calculation of the extent of effective protection for the refining activity is difficult in that much protection for refined sugar may be passed back to beet growers and extraction of raw where integrated beet sugar factories producing refined sugar are operating. Also if any substantial sugar importer changed from imports of raw to refined, this action would increase considerably the actual raw/refined margin on world markets.

[20] Total exports are limited under the provisions of the International Sugar Agreement.

what appeared to be a promising approach to industrialization in the developing countries".[21] It may be noted that the Western World is not alone in such actions — the agreement by the U.S.S.R. to buy Cuban sugar at favourable prices relates to raw sugar only,[22] much of this being re-exported by the U.S.S.R. as refined.

Table 5 contains data relating to exports of raw and refined sugar for the Pacific Region and other countries for a number of years, while Table 7 shows the direction of exports, and average prices received, by the major Pacific Region exporters. It can be seen that what growth occurred in the quantity of sugar exported during the 1960s[23] was in raw sugar, and that little refined sugar was exported by Pacific Region countries.[24] Also it can be seen that all Pacific Region exporters have access to preferential markets and receive average prices well in excess of the average price quoted for the world free market (1.9 c/lb. f.o.b. Caribbean Ports in 1968). Average receipts for Mexico, Peru and the Philippines also exceeded those for all (world) exporters as a whole, due to the substantial access of these countries to the U.S.A. market.

I have estimated elsewhere[25] the effects on export receipts of a complete removal of all protection (national and international) of sugar production and of taxation of sugar consumption. Using 1959-1961 as a base — and the present situation would differ little — it was estimated that on "universal free trade" assumptions and a world raw price of 4¼ c/lb. f.o.b. Caribbean, exports could be increased to the E.E.C., Japan, U.S.A. and U.K. by perhaps seventy-three per cent. This would imply additional export revenue (mainly to cane sugar exporters) of about $480 million per annum if the additional exports were all of raw sugar, or $780 million if they were refined; if the same proportionate increase in trade occurred in the rest of the world then the additional exports would have been $820 million or $1,350 million per annum, respectively. It can be seen that this estimated "universal free trade" export price of 4¼ c/lb. raw for 1968, would have implied a lower average export price for the Philippines, Peru and Mexico, but higher for China (Taiwan), Colombia, Fiji and Australia. For all there would have been the opportunity of substantially increased sales — though these would not have compensated for the reduced price for the Philippines, Peru and Mexico. Many countries may feel they would be subjected to reduced external political pressures if they could substitute a buoyant free market for dependence on the United States Sugar Act.

3. Other Tropical Products

We now consider trends in the exports of three other processed products of importance to tropical countries of the Pacific Region. First, wood and processed wood.

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[21] Donald C. Horton, "Policy Directions for the United States Sugar Program", *American Journal of Agricultural Economics*, May 1970, p. 193.

[22] Hallmans and Ivanov, *op. cit.*, p. 47.

[23] The total quantity exported (net, raw and refined) for the last four years of the 1960s exceeded that exported for the first four years of 1950s by about 40 per cent; however the last four years of the 1960s exceeded the first four years of the 1960s by only two per cent — a considerable reduction in 1969 being due to the imposition of export quotas under the International Sugar Agreement. (Calculated from data in International Sugar Council, *Sugar Year Book*).

[24] The division into raw and refined is not available prior to 1963.

[25] R. H. Snape, "Sugar: Costs of Protection and Taxation", *Economica*, February 1969, pp. 29-41.

As can be seen from Table 8, wood is an important export for many countries of the region.[26] In most of the countries there has been a substantial increase in exports, but this growth has been mainly in roundwood. Data in Tables 1 and 2 suggest that all relevant stages of timber processing are labour intensive, so that wood processing should be a suitable activity for developing countries. Table 3 indicates that processed wood products are discriminated against by major importers, as compared with the raw product, but Balassa states that "tariff differentials between sawnwood and roundwood are generally offset by differences in transportation costs."[27] If this is so (though it is doubtful whether it is in the case of Japan), there appears to be good prospects for exporters to move increasingly into sawnwood. Data in Table 9 show that during 1967 and 1968 almost five-sixths of the world's exports of coniferous logs and sawnwood occurred in sawnwood while less than a third of non-coniferous timber in these forms was exported as sawnwood.[28] As is shown by this table, the non-coniferous wood is of export importance to the less developed market economies whereas coniferous is mainly exported by developed market, and centrally planned, economies. Table 8 shows that while Europe and the United States, and particularly the latter, import a considerable proportion of wood in sawnwood form, Japan — whose imports of timbers have been growing very rapidly — takes nearly all its supplies as roundwood.

Japan's imports of non-coniferous timber are drawn largely from the Pacific Region, which region in turn directs most of its roundwood exports to Japan. Thus, as trade flows exist at the present time, a movement out of roundwood and into sawnwood by Pacific Region exporters will depend on Japan changing the composition of its imports. Balassa has calculated[29] that Japan, under the Kennedy-Round tariff reductions, is lowering the effective rate of protection on the sawing activity from 13.3% to 8.5%, the latter figure being that given in Table 3: it remains to be seen whether this reduction will be sufficient to increase its imports of sawnwood significantly.

European countries and the U.S.A. have provided, relatively, a better market for non-coniferous sawnwood. Western Malaysia and Sabah, the largest sawnwood exporters of the Region (excluding Japan), have obtained markets throughout the western world: if Japan does not change the pattern of its imports, these other markets should provide outlets for expanded exports of sawnwood. The additional return on such exports is indicated in Table 8: in terms of roundwood equivalent, the price received for non-coniferous sawnwood during 1967 and 1968 exceeded that for logs by about a third.

Table 8 also shows that the return on exports of veneer sheets or plywood is substantially greater than for roundwood or sawnwood; however the tariffs on veneer and plywood imposed by the countries that comprise the major potential markets are significantly greater than on roundwood or sawnwood. Despite these tariffs, four countries in the region (China (Taiwan), South Korea, Philippines and Japan) have built up worthwhile export markets in plywood and one (Philippines) exports veneer. All these exports depend heavily on one market — the United States. In the case of the Philippines, preferential treatment is accorded by U.S.A., but the other

[26] All data in Tables 8-11 are two-year averages.
[27] Balassa, *op. cit.*, Ch. III, para. 38; see also *ibid.*, Ch. I, footnote 12.
[28] The ratios are calculated on a roundwood basis.
[29] Balassa, *op. cit.*, Appendix Table A.

exporters have surmounted the tariff barrier. In each case (except the Philippines) the export of plywood is based on imported roundwood, so it might be expected that this processing activity will develop in other countries of the region. It has been argued that new techniques in plywood and veneer manufacture should aid the establishment of these processing activities in the less developed countries: briefly, they permit the utilisation of smaller girth and lower quality logs.[30]

In summary it would seem that the prospects for increased exports of processed non-coniferous wood are bright and that import demand for both raw and processed products should continue to expand rapidly.

Data regarding exports of coconut and oil palm products, for the major exporters of the Region, are contained in Tables 10 and 11. In palm oil, international trade occurs only in the oil and not in the product from which it is extracted (the outer pulp), as the oil must be extracted soon after harvesting. With palm kernels and copra, however, there is a choice for the location of oil extraction and the main part of international trade occurs in oilseeds rather than oil. Western Malaysia and Singapore (who are now net importers of copra) have increased coconut oil exports considerably over the period covered in Table 10. The Philippines is easily the world's largest exporter of both copra (mainly to Western Europe) and coconut oil (mainly to the United States, where it has, subject to a quota, duty-free entry[31]) and while exports of the former have declined, exports of the latter have increased. For palm kernels, the proportion of world exports taking the form of kernel oil has increased, though this development has not spread to the Pacific Region to any extent.

The processing of these oilseeds, unlike that of timber, is not clearly suited to the less developed countries. Tables 1 and 2 suggest that vegetable oil mills use a substantial quantity of physical capital per employee. Also, if oil cake, as well as oil, is exported there is little loss of weight in processing so that transport costs do not favour location in the exporting countries. (One may wonder why, in these circumstances, effective rates of protection of the crushing activities are so high in importing countries — Table 3. It may perhaps be relevant that these high effective rates are generated by low nominal rates, together with low value added in the crushing activity. They were not decreased in the Kennedy-Round.[32]) The paper submitted by the F.A.O. to UNCTAD I also contains doubts, based on grounds other than capital intensity, as to the wisdom of locating this processing activity in the exporting countries: "The decisive factor [in the profitability of crushing firms in developed countries] was success in buying and blending of materials, and in these operations crushers in developed countries have very marked advantages".[33] Further, advantages in the use of oil and cake in subsequent manufacturing processes appeared to lie with crushers in the developed countries. In short, processing of tropical oilseeds does not look a particularly desirable avenue of development for the major oilseed exporters.

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[30] F.A.O., *The State of Food and Agriculture*, 1969, p. 112.
[31] This quota will decline to zero by 1974. (B. Natapermadi, "The Plantation Crop Planting Industry in the ADB Region" in Asian Development Bank, *Asian Agricultural Survey* (University of Tokyo Press, 1969), p. 303.)
[32] Balassa, *op. cit.*
[33] *Op. cit.*, p. 167.

TABLE 1

Indexes of Value Added per Employee by Processing Industries — U.S.A. 1963

	Industry	Value Added per Employee	Payroll per Employee	Other Value Added per Employee
		Percentage of Average for All Manufacturing		
2013	Meat processing	102	101	104
2031	Canned and cured Seafoods	89	65	115
2033	Canned fruits and vegetables	89	63	116
2036	Fresh or frozen packaged fish	52	48	57
2041	Flour mills	147	104	193
2042	Prepared animal feeds	159	87	237
2043	Cereal preparations	284	112	470
2044	Rice milling	167	81	260
2061	Raw cane sugar	145	80	216
2062	Cane sugar refining	181	124	242
2091	Cottonseed oil mills	106	77	138
2092	Soybean oil mills	207	105	319
2093	Vegetable oil mills n.e.c.	193	100	294
2094	Animal and marine fats and oils	120	93	148
2095	Roasted coffee	317	110	541
2096	Shortening and cooking oils	173	111	240
2111	Cigarettes	325	87	583
2121	Cigars	82	56	111
2281	Yarn mills except wool	52	57	46
2282	Throwing and winding mills	61	59	63
2297	Scouring and combing plants	69	72	66
2298	Cordage and twine	57	66	48
2411	Logging camps and contractors	63	65	60
242	Sawmills and planing mills	57	65	48
2431	Millwork plants	71	83	57
2432	Veneer and plywood plants	75	83	65
2433	Prefabricated wood products	87	87	88
2611	Pulp mills	173	121	23
2621	Paper mills except building	126	115	139
2631	Paperboard mills	165	115	220
2661	Building paper and board mills	114	100	129
3111	Leather tanning and finishing	76	88	64

Source: United States Bureau of the Census, *Census of Manufacturers 1963*, Vol. II.

TABLE 2

Indexes of Value Added per Employee by Processing Industries — Australia 1967-68

Industry	Value Added Per Employee	Payroll per Employee	Other Value Added per Employee
	Percentage of Average for All Manufacturing		
Meat and fish preserving	103	96	110
Jam, fruit and vegetable canning	100	96	104
Flour milling	157	104	211
Animal and bird foods	167	102	234
Cereal foods and starch	133	97	170
Oils, vegetable	182	113	253
Boiling down, tallow refining	123	104	143
Tobacco, cigars, cigarettes etc.	607	101	1,131
Cotton ginning	358	158	564
Sawmills	79	89	72
Plywood mills (including veneers)	81	89	74
Tanning, currying and leather dressing	81	98	64

Source: Commonwealth Bureau of Census and Statistics, *Manufacturing Industry, Bulletin No. 5, 1967-68.*

TABLE 3

Nominal and Effective Tariffs in Selected Countries
After Kennedy-Round Reductions
Per cent

Commodity	U.S.A.		U.K.[a]		E.C.C.		Sweden		Japan	
	Nom.	Eff.	Nom.	Eff.	Nom.	Eff.	Nom.	Eff.	Nom.	Eff.
Meat										
Fresh and Frozen	4.6		4.2		17.8		0		6.2	
Preparations	4.7	5.6	8.3	10.4	19.5	44.3	0	-5.7	16.4	47.3
Fish										
Fresh and Frozen	1.3		6.0	14.9	14.9		0		5.3	
Preparations	4.9	11.0	8.8	13.1	18.7	35.8	3.7	8.6	12.0	27.5
Fruit										
Fresh	5.6		8.4		13.9		2.5		14.0	
Preserved	5.0	-4.9	5.3	2.9	20.6	28.9	10.3	21.8	31.8	56.7
Cocoa										
Beans	0		0		3.2		3.6		3.0	
Powder and Butter	1.6	11.6	0	-2.5	18.2	126.6	3.9	31.6	12.2	98.3
Chocolate	4.8	1.3	10.0	28.6	18.0	19.3	11.3	27.0	35.0	68.6
Leather										
Hides and Skins	1.1		0		0		0		0	
Leather	4.7	12.0	11.4	30.3	4.8	12.3	1.7	4.3	11.6	34.7
Leather goods ex. shoes	7.7	11.4	9.3	8.1	7.3	10.4	10.4	22.1	11.8	15.0
Shoes	14.9	26.3	20.4	32.7	11.9	19.3	11.9	22.8	22.9	36.5
Copra										
Copra	0		10.0		0		0		0	
Coconut oil (crude and Cake)	5.5	47.2	14.0	50.0	10.0	85.4	0	-1.0	10.0	85.4
Coconut oil, refined	30.0	30.0	15.0	15.0	15.0	186.3	0	0	10.0	10.0
Palm Kernel										
Palm Kernel	0	10.0	0		0		0		0	
Oil (crude and cake)	3.2	38.7	10.0	11.2	8.0	97.5	0	0	6.6	80.0
Oil, refined	2.4	2.4	10.0	10.0	15.0	186.3	0	0	8.0	8.0

Palm Oil										
Crude	0		10.0		9.0		0		8.0	
Refined	0	0	10.0	10.0	14.0	180.0	0	0	8.0	8.0
Rubber										
Natural	0		0		0		0		0	
Rubber products	4.6	6.6	10.9	22.5	7.9	16.3	6.6	16.1	6.4	10.3
Wood										
Rough	0		1.4		1.0		0		0	
Simply worked	0.3	0	6.3	18.8	1.6	4.0	0	0	2.9	8.5
Plywood	8.5	13.8	8.7	12.7	11.3	19.6	3.5	2.9	14.0	25.4
Manufactures	6.7	13.6	8.1	13.2	8.7	16.3	6.9	15.0	11.5	23.2
Pulp and Paper										
Pulpwood	0		0		0		0		0	
Woodpulp	0	-1.1	0	-2.4	3.3	-5.0	0	-0.5	5.0	7.5
Paper	2.5	5.0	5.8	12.7	6.1	13.0	1.0	2.0	7.7	17.2
Cotton										
Raw	6.2		0		0		0		0	
Yarn and Thread	10.5	25.0	6.1	19.3	10.0	32.9	8.7	30.4	2.8	6.8
Woven Fabrics	13.8	24.6	18.7	46.6	12.0	19.1	10.5	18.1	7.9	17.8
Clothing	20.0	35.4	20.0	28.6	14.0	20.8	12.4	19.7	14.7	27.5
Knitted Accessories	17.9	35.2	21.1	47.1	12.1	27.6	15.0	37.1	19.5	47.1
Jute										
Raw	0		0		0		0		0	
Woven Fabrics	0	-0.6	20.0	54.7	19.6	53.3	7.9	21.6	20.0	54.4
Sacks and bags	3.6	10.7	20.0	28.0	15.5	14.0	8.8	14.3	12.5	2.7
Sisal, henequen										
Sisal and henequen	0		10.0		0		0		0	
Cordage	3.6	10.3	10.5	21.9	10.3	30.6	10.4	32.2	9.6	28.1

[a] Tariffs on *Non*-Commonwealth imports.

Source: Bela Balassa, "The Structure of Protection in Industrial Countries and its Effects on the Exports of Processed Goods from Developing Countries" (Paper prepared at the World Bank for UNCTAD II, 1968), Appendix Table A.

TABLE 4

Nominal Tariffs on Selected Commodities

		Full	Commonwealth
United Kingdom[a]			
Coffee; unmixed			
(i) Roasted or ground	per cwt.	6sh. 3.6d	4sh. 8.4d
(ii) Other	per cwt.	4sh. 8.4d	Free
Coffee and chicory, roasted and ground, mixed	per cwt.	14sh.	12sh. 6d
Sugar: Raw	per cwt.	2sh. 0.7d-3sh.11.3d	Free
Refined	per cwt.	6sh. 10.8d	1sh. 0.8d
E.E.C.[b]			
Coffee: Unroasted		9.6-16.2%	
Roasted		19-22.8%	
Tea: In containers of 3kg. or less		11.5%	
Other		9%	
Cinnamon: neither crushed or ground		10%	
: crushed or ground		17.8%	
Cloves: neither crushed nor ground		15%	
: crushed or ground		20.8%	
Nutmeg: neither crushed nor ground		15%	
: crushed or ground		18%	
Cotton yarn: not prepared for retail sale		8%	
: prepared for retail sale		12%	
Silk cocoons		1%	
Raw silk (unworked)		5%	
Silk yarn: not prepared for retail sale		7%	
: prepared for retail sale		10%	
Silk fabrics		8-14%	
Japan[c]			
Coffee: unroaster		Free	
: other		35%	
Pepper: unground and unmixed		Free - 5%	
: ground or mixed		11%	
: put up for retail sale		19%	
Sugar: Raw		41.5 yen per kg.	
refined		51.5 yen per kg.	
Cube, loaf etc.		63.5 yen per kg.	

[a] Duties as at September 1969.

[b] Coffee, Tea, Cinnamon, Cloves and Nutmeg duties as at September 1969; others from January 1972.

[c] Duties during 1969.

Sources: Commonwealth Secretariat, *Industrial Fibres* No. 19 (1970) and *Plantation Crops* No. 13 (1970).

TABLE 5

Exports of Raw and Refined Sugar by Regions, 1963-1968
Thousand Metric Tons

Exported by:	1963	1964	1965	1966	1967	1968
Raw Sugar						
Pacific Region*						
Mexico	351	514	522	467	550	641
Colombia	42	31	102	114	176	237
Peru	493	425	362	430	475	467
China (Taiwan)	576	595	636	661	456	539
Indonesia	106	104	65	27	—	—
Philippines	1,048	1,082	1,017	929	926	886
Australia	1,148	1,124	1,279	1,258	1,647	1,601
Fiji	276	316	310	243	323	347
Other Central and North America	4,738	5,202	6,199	5,556	6,679	5,622
Other South America	884	552	1,152	1,406	1,444	1,549
Other Asia	259	242	340	518	220	171
Africa	1,639	1,659	1,555	1,822	1,878	2,114
Europe	599	478	694	595	422	507
World Total	12,159	12,324	14,231	14,028	15,196	14,680
Value ($U.S. million)	1,613	1,750	1,493	1,449	1,537	1,484
Refined Sugar						
Pacific Region						
China (Taiwan)	98	204	164	179	107	105
Central and North America	790	810	818	574	830	863
South America	334	47	63	24	39	66
China (Mainland)	200	330	367	442	338	211
Other Asia	610	460	331	277	198	188
Africa	70	74	48	51	108	121
U.S.S.R.	802	348	604	993	1,032	1,300
Other Europe	2,133	2,125	2,027	1,635	1,866	2,232
World Total	5,056	4,409	4,434	4,190	4,537	5,108
Value ($U.S. million)	800	759	405	323	348	391

*Countries are listed only if exports exceed 100,000 metric tons; Ryukyu Islands — Japan trade is treated as internal.

Source: F.A.O. *Trade Yearbook*, 1969.

TABLE 6

Average Prices for Raw and Refined Sugar 1963-1969

Year	ISC Average Price[a] Raw	Average Price Paid for Non-Preferential Raw Sugar[b]	Average Price Paid for Non-Preferential Refined Sugar[c]
	c/lb	Raw, c/lb	Refined, c/lb
1963	8.3	6.4	7.4
1964	5.8	7.5	8.6
1965	2.1	4.2	4.7
1966	1.8	3.1	4.1
1967	1.9	2.9	3.7
1968	1.9	2.9	3.7
1969	3.2	n.a.	n.a.

[a] An (unweighted) average of daily prices quoted by the International Sugar Council on an *f.o.b. Caribbean Ports* basis. It is derived from the spot prices quoted on the London and New York markets for "world" contracts.

Source: International Sugar Council, *Sugar Year Book*, 1969.

[b] Estimated average prices actually paid by importers of non-preferential raw sugar. It has been calculated by dividing the value of imports of raw sugar by all countries except U.K., U.S.A., U.S.S.R., Eastern Europe, China (Mainland), France and Portugal, by the quantity of imports of the same countries.

Source: F.A.O., *Trade Yearbook*, 1969.

[c] Estimated average prices actually paid by importers of non-preferential refined sugar. It has been calculated by dividing the value of imports of refined of all countries (except Bulgaria, East Germany, Poland, Romania and U.S.A.) by the quantity of imports of the same countries.

Source: F.A.O., *Trade Yearbook*, 1969.

TABLE 7

Direction of Exports of Sugar from Pacific Region Countries (1969) and Average Price Received (1968)

Exports To / Exports From	U.S.A.	Canada	U.K.	Japan	Other	Total	Average Price Received c/lb, raw
	Raw and Refined, Thousand Metric Tons, Raw Value						
Mexico	625	—	—	—	1	625	6.0
Colombia	80	7	—	59	27	173	2.6
Peru	268	—	—		—	268	6.1
China (Taiwan)	73	—	—	147	331	551	3.1
Philippines	1,020	—	—	—	—	1,020	6.6
Australia	177	171	362	437	384	1,531	3.1
Fiji	40	78	151	17	50	336	3.7
Total Imports from All Sources	4,432[a]	996	2,248	2,077	10,340	20,093[b]	4.3[c]

[a] Excluding Offshore Territories.

[b] World Total Imports.

[c] Average export receipts for all exporters of raw and refined, converted to a raw weight basis; on raw exports only the average price received was 4.6 c/lb.

Sources: International Sugar Council, *Sugar Year Book*, 1969, and F.A.O., *Trade Yearbook*, 1969.

TABLE 8

Wood and Processed Wood Exports and Imports
(Thousand Cubic Meters)

Country	Roundwood[a]		Sawnwood and Sleepers[b]		Veneer Sheets[c]		Plywood[d]	
	Av. 1959-1960	Av. 1967-1968	Av. 1959-1960	Av. 1967 1968	Av. 1959 1960	Av. 1967 1968	Av. 1959-1960	Av. 1967-1968
Pacific Region Exporters								
Colombia	54	42	32	80	—	—	—	1
Cambodia	62	91	4	8	—	7	—	15
China (Taiwan)	5[e]	40	36[e]	107	—	—	29[e]	341
Indonesia	146	1,314	12	10	—	—	—	—
Japan	32	64	401	361	35	5	389	381
Korea (South)	n.a.	—	n.a.	—	n.a.	—	n.a.	435
W. Malaysia	68	1,910	344	713	—	4	23	36
Sabah	1,625	5,558	30	4	1	8	—	10
Sarawak	365	2,618	207	293	1	8	—	10
Philippines	3,350	7,148	169	103	37	199	99	245
Thailand	54	31[f]	149	45[f]	—	—	—	—
Australia	27	34	111	68	1	1	—	2
Br. Solomon Is.	8[g]	80[f]	—	—	—	—	—	—
Papua-New Guinea	4[g]	191	10	17	—	1	11[g]	11
New Zealand	132	1,118	107	154	—	—	—	1

Total World Exports	20,960	55,581	39,432	52,055	320	832	1,570	3,433
Approx. roundwood equiv.	20,960	55,581	66,600	88,000	610	1,580	3,610	7,900
Value $U.S. m.	400	1,147	1,474	2,144	80	176	213	515
$ per cubic meter round wood equiv.:								
Coniferous	18[h]	20[h]	21[i]	23[i]	—	—	—	—
Non-Conif.	20[h]	25[h]	30[i]	33[i]	131	111	59	65
Major Importers								
Europe	11,615	13,498	22,885	29,032	140	255	760	1,618
U.S.A.	1,270	1,142	9,490	13,261	215	479	695	1,346
Japan	5,728	27,736	170	2,259	—	7	—	15

[a] SITC 241.1, 242.2, 242.3, 242.4, 242.9 (excludes pulpwood, exports of which from the tropical Pacific Region are negligible).
[b] SITC 243.1, 243.2, 243.3.
[c] SITC 631.1.
[d] SITC 631.2.
[e] 1958.
[f] 1967.
[g] 1959.
[h] Logs only.
[i] Sawnwood only.

Source: F.A.O., *Yearbook of Forest Products*, 1961 and 1969.

TABLE 9

Exports of Logs and Sawnwood
(Thousand Cubic Meters)

Exports by:	Year	Logs		Sawnwood	
		Coniferous (SITC 242.2)	Non-Conif. (SITC 242.3)	Coniferous (SITC 243.2)	Non-Conif. (SITC 243.3)
Developed Market Economies	Average 1959-60	2,330	1,223	26,626	1,918
	Average 1967-68	13,170	1,713	32,406	2,335
Developing Market Economies	Average 1959-60	90	11,281	1,283	2,680
	Average 1967-68	225	24,722	1,834	2,939
Centrally Planned	Average 1959-60	1,329	52	6,429	705
	Average 1967-68	2,553	214	10,920	1,657
World	Average 1959-60	3,749	12,556	34,338	5,302
Approx. Roundwood equivalent		3,749	12,556	57,300	9,600
	Average 1967-68	15,949	26,650	45,160	6,930
Approx. Roundwood equivalent		15,949	26,650	75,400	12,600

Source: F.A.O., *Yearbook of Forest Products*, 1969.

TABLE 10

Exports of Coconut Products
(Thousand Long Tons)

	Copra		Coconut Oil[a]	
	Av. 1958-1959	Av. 1968-1969	Av. 1958-1959	Av. 1968-1969
West Malaysia and Singapore	78	20[b]	54	60
Commonwealth Pacific Islands	92	89	19	17
Papua-New Guinea	67	89	24	22
Indonesia	168	230	—	12
Philippines	756	599	73	239
World Total	1,329	1,166	291	511

[a] The average extraction rate is 64%.
[b] 1969.

Sources: Commonwealth Economic Committee (Commonwealth Secretariat), *Vegetable Oils and Oilseeds* and *Tropical Products Quarterly*, and F.A.O., *Coconut Situation.*

TABLE 11

Exports of Palm Oil Products
(Thousand Long Tons)

	Palm Kernels		Palm Kernel Oil[a]		Palm Oil	
	Average 1958-1959	Average 1968-1969	Average 1958-1959	Average 1968-1969	Average 1958-1959	Average 1968-1969
West Malaysia and Singapore	22	32	—	1	79	302
Indonesia	34	48	—	—	116	160
World Total	768	400[b]	92	140[b]	586	640[b]

[a] The average extraction rate is 47%.
[b] 1968, estimated.

Sources: Commonwealth Economic Committee (Commonwealth Secretariat), *Vegetable Oils and Oilseeds* and *Tropical Products Quarterly*.

TWO COMMENTS BY A CANADIAN GOVERNMENT OFFICIAL WHO WAS UNABLE TO ATTEND

First, although there was a significant price decline in sugar during the 1960s, market conditions have changed somewhat since then. Secondly, many countries probably would not want to substitute a buoyant free market for dependence on the U.S. Sugar Act, contrary to Professor Snape, as long as the price in the U.S. was as good as any likely option.

DISCUSSION OF THE PAPERS

of

Dr. H. Vandendreissche and Professor R. H. Snape

Professor Snape, replying to the first comment on his paper, said that the annual average prices he quoted for recent years indicate that the refined/raw sugar margin has not changed. Secondly, although sugar-producing countries get higher prices under the U.S. Sugar Act than on the world market, he was upset by the 'imperialistic' provision (under the new U.S. Sugar Act) for reducing the price of sugar, or the receipts of the less developed countries, by a fixed amount (at the President's discretion) if any country seizes any property belonging to the U.S. and pays what the President regards as an unsatisfactory price. While granting that the sugar producers themselves suggested the new act, as one U.S. participant pointed out, Professor Snape emphasized that he was comparing the situation under the Sugar Act to a "buoyant" free market, not the present world market.

The complexities of analysing specific processing industries were emphasized throughout the discussion and in the case of sugar it was pointed out that the bulk of sugar is not traded on the European market but rather at long-term contract prices. Consequently, the prices for both raw and refined sugar that Professor Snape used were said to be marginal prices reflecting the dumping in many cases of East European and Cuban sugar on the West European market. This would partly explain why sometimes the refined sugar price was less than the raw sugar price.

With respect to Dr. Vandendreissche's theoretical discussion, one participant (from an international institution) pointed out that, on one hand while classical economic theory does say that firms will locate generally where it is most profitable, on the other hand it requires the assumption that capital markets be perfect. In developing countries this would imply that low per capita income and low capital accumulation would mean that capital is not available generally for specific processing activities. However, it was said that capital markets are not at all perfect, if they even exist, in these countries and a great deal of processing activity is linked to capital markets through the marketing organization. Thus the real issue was said to be whether the companies which process palm oil or timber, etc. decide to do it in the developed or the less developed country, for the technology and capital are linked to decisions about where the comparative advantage lies in a more basic sense related to ease of processing, transport and so on. It seems that there is ample capital available, for example, for oil or timber processing that simply would not be available for other types of activities, so that the opportunity costs of this capital are not those of capital for other activities in the economy. Along with Professor Safarian, many participants emphasized the importance of industry structure in affecting the location of processing.

The large, oligopolistic, multi-national corporations, which dominate many of the extractive and processing industries, tend to locate processing industries, tend to locate processing where it is most profitable and the most profitable location, dictated to an important extent by the framework of trade barriers, is now generally in Europe, the United States or Japan. In

the case of palm oil and copra it was mentioned that preferential access to the U.S. market for the Philippines has led to oil production in the Philippines and oil exports rather than copra to the U.S. whereas other Southeast Asian countries export mostly copra to be processed in the U.S. because they do not have preferential access. It was emphasized that the vertical integration of processing from growing or extracting to find processing and often marketing within the multi-national corporation results in a tendency to shift profits to the parent in the developed country by the corporations ability to fix raw material prices in a monopolistic way. This cuts into the element of economic rent that belongs to the less developed country by virtue of its owning the raw resources or tropical land. Thus the less developed country loses not only the advantages, whatever they are, of having the processing located there, but also some of its economic rent. This was said to be true of the edible oils industry and an example from the petroleum industry was described. A participant from the U.S. suggested it might be possible for the suppliers in less developed countries to cooperate as a cartel to counter these oligopolistic practices and force the developed countries to lower tariff barriers or discriminatory taxes. It was agreed that this would be relatively easy for extractive industries like petroleum, but it would be extremely difficult in processing industries.

There was little discussion of the interrelation between tariff distortions of trade and distortions due to oligopolistic industry structure. However, one participant from Canada said that because value-added by processing is in most cases very small it does not matter very much where the processing is located in terms of jobs or income. Then, since the processors in the developed country have a concentrated interest in protecting their business while consumers are relatively uninterested due to the small element of value-added, it is relatively easy for the processors to exert political pressure to institute or maintain tariffs, which themselves only need to be small to give high effective protection. This led to the view of this participant that, because of the monetarily small size of the value-added involved, the question of the location of processing was not a very important part of the problem of development. This participant agreed that the tariff policies of the advanced countries ought to be changed, but did not feel that this was a major element in economic development policy. Other Canadian and American participants disagreed with this view, however, and suggested that at least in some products there was considerable leverage involved in locating processing in less developed countries and that consequently the reduction of tariff barriers in both the developed and the less developed countries was an important element of economic development policy.

From the latter point of view, the participant from Singapore and a Canadian participant emphasized the importance to the developing countries of trying to fill in the structure of production, in terms of the cells of an input/output matrix and of developing the linkage and spillover effects of establishing processing activities and technological innovations in several key industries. The Canadian participant suggested that integrated development by planning several sectors at once is important, for example, by making use of by-products, such as molasses and alcohol in the case of sugar refining, that would otherwise be wasted. Other participants however mentioned that one of the problems with integrated planning in less developed countries is to find markets for all these by-products whereas the developed countries are rich enough to have markets for everything. It was also suggested that the location of processing activities in developing countries provides linkages through which external economies of scale may be transmitted or generated

and the establishment of a palm kernel crushing industry in Malaysia was cited as an example. Furthermore, the Singapore participant noted that with much un- and underemployment in many Pacific tropical countries, the opportunity costs of unemployed labour may be very low or zero so that processing would tend to be more profitable than otherwise. Finally, the Canadian participant felt that if processing activities are becoming foot-loose as suggested by Dr. Vandendreissche and if the cost economics expected from this are due to 'learning-from-doing' or a kind of Myndal 'backwash effect' of established locations, then the location of processing becomes a subject of international negotiation and in such negotiation the benefits of the infant industry argument should go to the less developed countries.

All participants agreed with the view that if the real rates of exchange, tariffs and export taxes and subsidies were correctly calculated, the less developed countries would clearly have a cost advantage in the location of processing activities. It was also clear that the tariff barriers of the developed countries are designed precisely to divert processing and manufacturing away from the less developed countries. Several countries have introduced preferential tariff schemes supposedly for the benefit of the less developed countries, however, the Japanese scheme affects only 3 to 4 per cent of total Japanese imports, the Australian scheme less than one per cent and the European. Economic Community has a scheme involving tariff quotas that ensure few benefits, especially to East and Southeast Asian countries. Moreover, it was explained that the commodities affected by the preferences are not the agricultural processed goods, but rather manufactured goods, although even here labour-intensive processed goods and sensitive goods like textiles are excluded. Thus, as one participant observed, in commodities where there might be some benefits from preferences, preferences were not given. A U.S. participant said that, at the time the U.S. decided to accept general preferences, it proposed, in the face of much internal political pressure, that processed agricultural goods be included, but the European Economic Community and Japan said that there was no possibility at all of this in the next decade. Later in the Conference the disadvantages of the U.S. scheme were also pointed out.

Another question asked was concerned with the degree of effective protection actually used by producers in terms of their pricing policies. The only evidence on this question was an aggregate study of the Australian manufacturing industry as a whole which had effective protection of 47% on average, but of this only about one-half was used, although this figure was probably biased downwards.

While the participants as a group thought tariffs to be a very important factor in distorting trade patterns and thought they ought to be removed, it was difficult to answer the question whether they are *by far* the most important distorting factor. One participant from Canada answered that while tariff policies do distort the location of industry in ways which are harmful to the less developed countries, there are other aspects of economic policy and economic organization which might well survive the tariffs and give the same effect. For example, once a country begins by having a corporate income tax, an element of irrationality is thrown into the location of industry right away. Consequently, the problem of rationalizing the location of industry is not one that can be simply solved by taking down tariff protection. It was said that the structure of wages and costs adjusts to the tariff system. It is easy enough to look at one industry such as sugar refining, calculate that it has effective protection of so much and then predict that if

the tariff were taken off that industry only, it would disappear. However, besides questions of tax and non-tariff barriers and industry structure, it would be difficult to predict the results if all tariffs were taken off simultaneously. Partly because of the fixed capital and labour to some extent is protected industries, it was said that, if tariffs were removed simultaneously, it is possible that the exchange rate adjustment that would have to be made to match it would leave the country with much the same industrial structure as before the change, although there would be some reshuffling of resources.

At the end of the session Dr. Vandendreissche commented that the whole discussion seemed to have begged two questions. First, what in fact is the cost of all these elements, of protection that have been discussed? These he tried to discuss in his paper. Secondly, what are the rich nations within the region willing to do to help bring about a new international division of labour, at least within the region. For example, he suggested that some long-term purchasing agreements, such as some Japanese firms have made, along with aid to developing countries, would be a large contribution to solving some of the problems created by tariff barriers.

A REVIEW OF SOME BASIC PROBLEMS OF THE KENAF FIBER INDUSTRY IN THAILAND*

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Introduction

Kenaf, or "Thai Jute" is the common name of two closely related species of the family Malvacaeae, Hibiscus cannabibus and Hibiscus sabdariffa. Thailand and India are the two major producers of this agricultural fiber, although the former is by far the largest exporter of the product.

Almost all of the kenaf grown in Thailand is Hibiscus sabdariffa var. altissima, and essentially tropical crop. The species withstands drought and can be grown where there is little rainfall. However, there should be sufficient moisture at planting time so that germination is not impeded. For this reason, the planting of kenaf begins early in the rainy season, i.e. between May and June, and some 140 - 160 days later, in September and October, when the plant grows to a height of 4 to 12 feet or more, depending upon climatic conditions, soil fertility and time of planting, it is harvested. Kenaf, as an upland crop, is grown abundantly in the Northeast region.

Botanically, kenaf is different from jute (Corchorus capsularis and Corchorus olitorius). Although the soft fiber contained in the bast of the stalks has properties very similar to those of jute fiber and could be used as a jute substitute, jute fiber is inherently finer than that from kenaf and can be used to make finer yarns. Because of this inferior natural quality, kenaf if much cheaper than jute in the market.

Before 1950, the commodity was of little commercial significance, but since then production increased steadily, reaching its peak in 1966 when the total output amounted to 661,000 metric tons of fiber, and earned for Thailand $ US 80 million from exports. In that year, kenaf came third, after rice and rubber, on the country's export account. In recent years, both production and exports have substantially declined to an average of 250,000 - 350,000 metric tons. Nevertheless, Thailand still manages to maintain her position as the world's largest producer and exporter.

In view of the fact that kenaf not only contributes significantly to the growth of the Thai economy, but also serves as a major Thai contribution to world supply of industrial raw materials, the present paper aims at reviewing some basic problems confronting the kenaf fiber industry and, as far as possible, suggesting a broad approach for future policy formulation.

In many ways, the author is indebted to various publications and memoranda written on the same subject, such as UNIDO's "Report on the Kenaf Industry in Thailand", Erwin J. Sholton's "Kenaf in Thailand", and Eldon D. Smith's "Government Policies for the Thai Kenaf Industry and Economic Analysis, which have enlightened him on several technical points. A selected bibliography is attached.

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*This paper has been prepared for the Fourth Pacific Trade and Development Conference, held in Ottawa, Canada, on October 7 - 10, 1971.

TABLE 1

Estimated World Production of Jute and Allied Fibers*
1960/61 – 1970/71

	1960/61-1962/63	1963/64-1965/66	1966/67	1967/68	1968/69	1969/70	1970/71
	(1,000 Metric Tons)						
Jute							
Pakistan	1,027	1,022	1,170	1,157	1,036	1,290	1,184
India	944	992	995	1,128	524	1,088	900
Brazil	45	52	44	40	51	32	45
Nepal	40	39	38	40	30	35	35
Burma	7	12	13	18	21	22	24
Thailand	8	8	11	10	10	10	10
Others	122	151	175	122	191	201	199
Total	2,193	2,276	2,446	2,515	1,863	2,598	2,397
Kenaf & other Fibers							
Thailand	184	348	661	421	317	350	370
India	270	282	218	227	162	108	270
Pakistan	36	42	65	53	23	40	41
Brazil	13	14	17	14	18	18	26
Indonesia	4	5	8	16	13	17	16
Others	34	37	42	36	48	48	51
Total	541	728	1,011	767	581	581	774
Grand Total	2,734	3,004	3,457	3,282	2,444	3,179	3,171

*Excluding production in centrally planned countries, namely, USSR, Mainland China, and North Vietnam.

Sources: FAO's "Study Group on Jute, Kenaf and Allied Fibers" (CCP:JU/CC 71/3), Bank of Thailand.

The General Problem

Kenaf is of considerable importance to the economy of Thailand; past, present, and future. Its importance derives from the following elements.

First, kenaf is the major cash crop of the farmers in Northeast Thailand where rice is cultivated mainly for family consumption. Being an upland crop, kenaf could be grown in the areas which are not suitable for rice cultivation. It is also a more profitable crop than rice. The total annual income derived from kenaf cultivation at the level of 400,000 metric tons per season could be as high as $ US 40 million (or about Bht. 800 million) which obviously helps raise the average income of those poor farmers above its subsistance level. This is a significant consideration in view of the need to improve the Northeast income which is at present much lower than the national average.

Secondly, the development of the kenaf industry in the Northeast has generated employment within the regionso that not only is the utilization of manpower between rice crops improved but also new jobs have been created for the rapidly increasing agricultural population. Additional employment generated by the industry consists of activities in about 200 baling plants (over 30,000 jobs) and those in the ten jute mills (over 15,000 jobs) located mainly in the same region. Kenaf baling and processing are the only major industrial activities in Thailand's Northeast which together contribute between $ US 10 - 15 million or about Bht. 200 - 300 million to the GNP.

Finally, Kenaf fiber is one of the major export items of Thailand. At its peak in 1966, kenaf came third after rice and rubber, earning for Thailand $ US 80 million or Bht. 1,614 million, or about 11% of the total export value of the same year. Today, after a decline in both output and export, kenaf fiber still ranks high among individual export products, with a contribution of over 5% in value. In addition to that, exports of finished products made of kenaf such as gunny bags and hessian cloths are also rising, earning for Thailand additional foreign exchange to pay for her rapidly increasing imports of capital goods and other industrial raw materials necessary for the country's industrialization program.

Economically important as it is, the development of kenaf industry in Thailand is still far from being satisfactory. The industry has been encountering many serious problems which impede its further growth.

The kenaf problems, regardless of their derivatives, focus on a single factor, namely, *an extremely unstable price.*

The extreme instability in prices is responsible for wide fluctuations in the fiber's output, for uncertainty in the kenaf processing activities, and to a great extent, for the lack of quality improvements. The fluctuation in the fiber's output of some 100,000 metric tons or more from year to year not only affects the stability of income, employment and foreign exchange earnings, it also creates further price uncertainty for the raw material and so upsets the production programming of the related processing industries both to meet the requirements of the domestic market and export commitments.

The problem of price instability undoubtedly originates from the characteristics of the fiber's international market itself.

The demand for kenaf is primarily international. Domestic consumption, though growing, accounts for less than 100,000 metric tons per year, which is the amount required to meet the needs of local jute manufac-

turing, a primarily import-substitution industry with surplus capacity for export. Under these circumstances, fiber output above 100,000 tons for any given year will have to find a market abroad. This excess of output has ranged from 100,000 tons to 500,000 tons, depending on the size of the crop in any particular season.

It should be pointed out that kenaf forms only a relatively small part in the total world supply of coarse fibers, more or less about 20 per cent. Therefore, in the international market, kenaf has to compete with jute which is not only regarded as a superior product, but in fact occupies the remaining 80 per cent of the total world supply. It must also be noted that the role of kenaf is only that of a limited substitute of jute. In many uses, jute and kenaf fibers are mixed or blended, the proportion varying with use and local practice, mainly for the purpose of lowering the cost of production. Nevertheless, experts have contended that despite some natural inferiority, kenaf fiber of uniform quality can be substituted almost completely in some of the major uses for jute of the lower grades. Gunny bag manufacturing is a clear example of complete substitution.

The toughness of competition in the world market become clearer when account is taken of the fact that Thailand is not the sole supplier of kenaf, although it is by far the largest.

Competition with jute is however, only a part of the story. In reality, both jute and kenaf, together with the other natural coarse fibers, have also been facing competition from a group of potential substitutes, consisting of paper synthetic fiber, sheet plastics, and to some extent cotton, under certain conditions, which have already captured part of the market. In this connection, the role of kenaf is rather unique, for its relatively low price has helped meet the threat of these potential substitutes as the supply of kenaf at low prices has enabled the spinners to use it in admixture with jute and thus lower their raw material cost.

With the characteristics of the international market as described above, it is apparent that price instability is hardly avoidable. Year-to-year changes in average wholesale prices of kenaf have averaged some 28 per cent during 1951 - 1956, and the range of monthly average prices between 1963 - 1968 has been more or less on the same scale. In 1970, a relatively normal year, the price of Grade A kenaf fluctuated between £ 78.0.0 and £ 93.10.0, a ton Grade B between £ 73.0.0 and £ 89.10.0, and Grade C between £ 65.0.0 and £ 83.0.0 respectively, all quoted in the London market.

The fact that kenaf prices are low relative to those of jute does not present itself as a real problem to the kenaf industry, although higher prices would encourage expansion in production and help improve income and employment as well as export earning. As already stated above, the crux of the problem lies in the fact that the existing low prices fluctuate widely from year to year, from month to month, and from week to week. In other words, whereas low prices can be taken for granted if price stablility exists, and fluctuations, on the other hand, are acceptable if risks could be compensated by higher prices, the combination of low and extremely unstable prices is absolutely intolerable under any circumstances.

The general problem, therefore, seems to be how to remove at least one of the adverse factors from the scene, so that Thailand could confidently continue to supply kenaf fiber to the world, and in return, acquire growth and stability for her own economy.

Production of Fiber

Kenaf is mainly grown in an area bound by the Provinces of Udorn, Korat, Ubold, and Chaiyaphum in Northeast Thailand. The soil in the region is sandy, well-drained, and particularly suitable to the plant. During the 1970/71 season, the area devoted to kenaf cultivation is estimated at approximately 2.4 million rai or 960,000 acres, with some 400,000 rai or 160,000 acres increase over the last season. Although the yields obtained tend to vary from one specific location to another, with 500 kilograms per rai as highest, they have in recent years averaged between 150 - 200 kilograms per rai in most of the areas under cultivation. The relatively low yields on the average is due to many factors including the use of seed with poor germination rates, insufficient preparation of the soil, and the lack of line sowing and consequent improper spacing.

Thai kenaf is considered to be of inferior quality and to lack uniformity. One of the reasons for poor quality is that whenever labor is required for rice and kenaf operations at the same time, rice, being the food crop, is given preference. Kenaf is therefore often left unharvested past its maturity, thus producing poor quality fiber. There is also a problem of shortage of clean water for retting and washing the fiber after harvesting. This problem can become acute particularly when plants are harvested later than they should be. In Northeast Thailand, kenaf is retted wherever water is available for the purpose, such as swamps, ponds, road-side ditches and streams. The lack of suitable retting facilities and of water at the time it is required, experts have agreed, constitutes the single most serious problem as far as the improvement of the quality of Thai kenaf is concerned.

Other factors contributing to the poor quality of Thai kenaf include too early removal of the stalks from the water at the end of the retting process which leads to barky runners and an excessive amount of unretted butt-ends to be left on the fiber, too late removal which causes over-retting and weakening of the fiber, improper washing after stripping, and careless spreading and alignment of the fiber on the drying lines. All these shortcomings could be removed, if the farmers had an economic incentive in the form of price differential between grades to do so.

Between 1956 - 1966, kenaf output grew steadily from 17,000 metric tons to 661,000 metric tons, but since then it has declined to a level of around 350,000 - 400,000 metric tons. Table 2 below gives details on kenaf and jute outputs since 1950.

Fiber Grading

In practice, the farmer does not grade his fiber. As the fiber is sold in "mixed grade", the farmer not only has no incentive to exert an extra effort to produce superior quality fiber, but it is also to his own interest to try to deliver as low quality fiber as he possibly can. Pre-grading on the part of the farmer, no matter how necessary for the improvement of the quality, is practically ruled out because of the lack of economic incentive in terms of price differential between grades.

The first actual grading of the fiber is therefore carried out by the baling plants which at present number more than 200 and are mostly located in the kenaf areas of the Northeast. The average size plant is capable of handling some 4,000 - 6,000 tons of fiber per season. After grading according to quality, the under-retted butt-ends are removed, and the remaining fibers

TABLE 2

Thailand's Production of Jute & Kenaf, 1950 — 1970

	Kenaf	Jute
	(Thousand Metric Tons)	
1950	4.7	2.5
1951	20.0	3.0
1952	13.1	1.0
1953	14.0	1.8
1954	8.2	1.3
1955	9.8	1.3
1956	17.0	2.5
1957	21.0	2.8
1958	29.6	2.9
1959	50.0	3.9
1960	181.3	6.2
1961	239.0	11.6
1962	134.0	6.7
1963	211.7	6.9
1964	303.1	6.5
1965	528.6	8.7
1966	661.4	10.9
1967	421.4	7.4
1968	316.8	4.4
1969	350.0	10.0 (estimated)
1970	370.0	10.0 (estimated)

Source: Ministry of Agriculture.

are compressed into 180 kilogram export bales by high-density presses. As the primary responsibility for grading rests with the baling plants, after which the fiber will be sent to the jute mills for manufacturing or to Bangkok for export, the activities of these plants are of paramount importance. Unfortunately, partly owing to lack of experience or neglicence and partly to fraudulent practices, some balers do not adhere to the official grading standards. For this reason, much of the fiber, reaching exporters and the mills is of poor-uniform quality, with consequent harm to the reputation of Thai kenaf in the international market.

The importance of serious grading is however not overlooked by the Government, and, in fact, serious efforts have been made to overcome the poor quality problem. Before shipments, inspections are carried out by the Office of Commodity Standards to determine whether the quality and packing of the fiber conform to the standards laid down by the Government.

According to the official standards, kenaf is classified into four grades, namely, Super, A, B, and C, each of which must be strong with a

maximum limit of moisture content of 14 per cent by weight. Fiber of super grade must be sheeny white in color and very soft with a minimum length, i.e. 1.00 meter, but Grade A is whiter and softer. In addition to that, fibers of Super Grade and Grade A, must contain no hard root and top ends, whereas for Grade B, the hard root, if any, must not be longer than 10 centimeters. Grade C fiber is, of course, of inferior quality. Standards inspection is made on the minimum basis of 5 per cent of the total number of bales to be certified. The work of the Standards Office is supported and assisted by the Thai Jute Association which recently has amalgamated with the Thai Jute Balers Association, both of which represent the private sector.

The grading problem therefore lies more on the practical side, i.e. how to make the actual practice conform to the official standards requirement. It has been suggested that perhaps the most logical approach is to pay attention to grading from the beginning of the process until the end of the line, i.e. from the farmer to the exporter. Whereas some economic incentives have to be provided for the farmer to pre-grade his fiber, it is the baling plants in the up-country that have to be placed under strict control and supervision.

Fiber Manufacturing

Part of the kenaf fiber produced is consumed within the country. The annual demand for 100,000 metric tons comes directly from the ten jute mills, most of which are located also in the Northeast, and three of which are government owned and operated. These mills were primarily established to manufacture gunny bags to substitute for imports which prior to 1952, when the first mill was set up, amounted to 30 million units. The local jute mills vary in size and capacity, but all together are capable of producing some 80 million units of gunny bags per year. Since local consumption amounts to only 40 - 45 million units annually, the gunny bag industry has in recent years been facing a serious problem of over-production. In 1968 when the total output of gunny bags was as high as 60 million units, over-production led to a sharp fall in prices. For months, the price of the standard rice bag (size 29" x 43") averaged as low as Bht. 4.50 per unit which was somewhat lower than the average cost of most, if not all, of the jute mills. The problem of over-production and depressed prices made it necessary for the mills, both private and government alike, to come together and form a "Jute Mill Group" with the purpose of regulating the production of each of the mills within the limit of the current domestic requirements, as well as the prices. Since the formation of the "Group", the industry has been able to gradually raise the domestic prices of its products to a profitable level. The gain derived from domestic sale is intended to serve as a compensation for the loss incurred from export. Since July 1971, supported by a stronger export demand partly as a result of the recent Pakistan political crisis, the domestic price for gunny bags has been maintained at a high level at Bht. 8.30 per unit. At this price, an average mill could make a profit between Bht. 1.50 - 2.50 per unit, depending on the mill's efficiency and, of course, the prevailing prices of kenaf. At the same time, export prices have also gone up considerably, from a normal level of about Bht. 5.00 - 5.50 per unit on the average to that between Bht. 8.00 - 8.50. For the time being, the industry is definitely enjoying a rare moment of comfort.

Apparently, Thailand's gunny bag industry's fundamental problems are excess capacity and consequently, over-production; both factors tend to keep the cost per unit higher than otherwise. Considering the fact that the

average Thai jute mill is of relatively small size, excess capacity for each individual mill and over-production for the whole industry together, present no easy problem. The only realistic solution is therefore to be found in an adequate export program.

Given the annual domestic requirement of gunny bags at 40 million units, the industry has at its disposal between 30 - 35 million units which can be offered for sale in the international market. With full capacity production, the cost per unit is likely to be more competitive, and product diversification on the part of the industry itself could further widen the market. In other words, export expansion of kenaf products is still a strong possibility. The only difficulty, however, is the extremely unstable price of, the raw material, kenaf.

Price instability which renders export programming ineffective and longpterm commitments impractical is illustrated in the following tables. It can be seen that not only have fluctuations occurred from year to year, but even from month to month (or from week to week); wide fluctuations in the kenaf prices are regarded as a normal phenomenon. These fluctuations make it almost impossible for the jute mill to quote any price which is effective over a few weeks. Recently, many Thai jute mills have incurred heavy losses despite specially strong export demand. The losses are due to the fact that export contracts were signed early in the year when the average price of kenaf was still around Bht. 3.00 per kilogram and the price of the finished product was quoted and agreed to accordingly. But at the time of manufacturing and delivery, the kenaf price has already gone up by almost Bht. 1.00.

TABLE 3a

Average Monthly Ex Godown Prices of Baled Thai Kenaf, 1963 — 1971*

	Grade A							
	1963	1964	1965	1966	1967	1969	1970	1971
January	4.05	3.42	3.65	4.17	3.67	3.75	3.00	3.30
February	3.77	3.50	3.60	4.30	3.55	3.70	3.10	3.05
March	3.37	3.45	3.50	4.50	3.32	3.55	2.90	3.05
April	3.20	3.42	3.77	4.62	3.05	3.35	2.85	3.75
May	3.32	3.30	3.87	4.77	2.80	3.10	2.90	
June	3.42	3.22	4.15	4.60	2.65	2.75	3.15	
July	3.45	3.12	4.12	4.40	2.70	2.75	3.00	
August	3.30	3.77	3.97	4.12	2.80	2.70	2.75	
September	3.07	4.10	3.97	3.55	2.65	2.70	2.85	
October	2.97	3.85	3.75	3.40	2.62	2.35	3.15	
November	3.10	3.67	3.85	3.55	2.55	2.50	3.35	
December	3.22	3.65	4.00	3.60	2.52	2.75	3.35	

*Bht. per kilogram.

Source: Thai Jute Association.

TABLE 3b

Average Monthly Ex Godown Prices of Baled Thai Kenaf, 1963 — 1971*

Grade B

	1963	1964	1965	1966	1967	1969	1970	1971
January	3.75	2.95	3.37	3.77	3.25	3.55	2.75	3.10
February	3.55	3.02	3.30	3.92	3.15	3.50	2.90	2.85
March	3.10	3.02	3.05	4.17	3.42	3.30	2.65	2.75
April	2.87	3.02	3.25	4.42	2.65	3.05	2.50	3.35
May	3.10	3.02	3.42	4.62	2.40	2.85	2.55	
June	3.27	3.00	3.80	4.45	2.10	2.55	2.80	
July	3.32	2.97	3.82	4.12	2.10	2.55	2.65	
August	3.20	3.60	3.72	3.90	2.20	2.50	2.45	
September	2.92	3.82	3.70	3.40	2.05	2.45	2.55	
October	2.80	3.57	3.52	3.15	2.17	2.20	2.85	
November	2.80	3.42	3.52	3.25	1.92	2.30	3.15	
December	2.77	3.35	3.57	3.25	1.75	2.50	3.15	

*Bht. per kilogram.

Source: Thai Jute Association.

TABLE 3c

Average Monthly Ex Godown Prices of Baled Thai Kenaf, 1963 — 1971*

Grade C

	1963	1964	1965	1966	1967	1969	1970	1971
January	3.20	2.55	3.05	3.20	2.80	3.15	2.25	2.80
February	3.10	2.80	2.92	3.12	2.67	2.65	2.45	2.45
March	2.67	2.85	2.67	3.25	2.35	2.65	2.30	2.25
April	2.75	2.82	2.80	3.62	2.07	2.30	2.00	2.75
May	2.92	2.85	3.05	3.82	1.80	2.20	2.00	
June	3.05	2.75	3.50	3.50	1.70	1.90	2.35	
July	3.02	2.62	3.60	3.20	1.70	1.90	2.20	
August	2.92	3.22	3.52	3.00	1.70	1.90	1.95	
September	2.67	3.52	3.52	2.77	1.55	1.90	2.05	
October	2.52	3.27	3.25	2.70	1.60	1.65	2.40	
November	2.45	3.10	3.05	2.82	1.30	1.80	2.80	
December	2.42	3.07	3.05	2.82	1.10	2.00	2.90	

*Bht. per kilogram.

Source: Thai Jute Association.

Following the development of the kenaf fiber industry, the output of gunny bags climbed steadily during the 1960's, reaching its peak of 55.2 million units in 1968. The bags themselves are manufactured in various sizes according to market demand, but the most common is the 100 kg. rice sack of 29" x 43". Apart from bags, some mills also produce hessian cloth and twine which, despite a relatively limited market, are more profitable than bags. Table 4 below gives the annual output of gunny bags between 1961 - 1970.

TABLE 4

Production of Gunny Bags, 1961 — 1970

	Output (Units)
1961	8,842,091
1962	10,815,942
1963	23,128,987
1964	33,511,424
1965	40,360,865
1966	46,807,019
1967	54,661,099
1968	55,284,099
1969	44,893,638
1970	52,733,326

Source: Bank of Thailand.

Export of Fiber

Thailand began her export of kenaf fiber in the 1959's, but it was not until the early 1960's that the product come to be considered one of the major export items of the country. Table 5 shows export quantity and value between 1958 - 1970.

In addition to kenaf, there has also been a small export trade in jute. In 1970, for example, jute exports amounted to 3,595 metric tons valued at Bht. 9 million.

Kenaf fibers exported from Thailand are of several grades, namely, Grade Super, Grade A, Grade B, Grade C, and Cuttings and Tangles. Table 6 provides data on exports by grades during 1966 - 1971.

It should also be noted that owing to the practical problems of control and supervision already referred to, Thai kenaf of Grade Super and Grade A may not be consistent with international standards. However, most of the exports consist of relatively high grade fibers which serve as substitutes for jute, whereas gunny bag manufacturing normally requires a higher proportion of fibers of lower Grades.

Thailand's customers are distributed all over the world. From Western Europe, there are Belgium, Italy, France, Federal Republic of

TABLE 5

Kenaf Exports of Thailand, 1958 — 1970

Year	Quantity (1,000 Metric Tons)	Value (Millions of Baht)
1958	27.5	69
1959	36.5	86
1960	60.8	227
1961	142.4	623
1962	236.7	575
1963	124.9	356
1964	161.8	494
1965	316.8	1,102
1966	473.0	1,613
1967	316.8	865
1968	289.2	674
1969	254.6	776
1970	251.3	677

Source: Department of Customs.

TABLE 6

Exports of Thai Kenaf by Grades 1966 — 1971

Year		Super	Grade A	Grade B	Grade C	Others
				(Metric Tons)		
1966		2,751	157,706	146,953	115,716	62,156
	% of total	(0.57)	(32.50)	(30.28)	(23.85)	(12.80)
1967		2,378	119,077	91,332	67,234	44,205
	% of total	(0.73)	(36.73)	(28.17)	(20.74)	(13.63)
1969-1970		2,920	143,247	69,102	27,150	39,492
	% of total	(1.04)	(50.81)	(24.51)	(9.63)	(14.01)
1970-1971 (to April 1971)		1,088	86,462	41,237	19,221	23,930

Source: Thai Jute Association.

Germany, United Kingdom, Portugal, Spain, the Netherlands, and Rumania represent Eastern Europe among the customers. In addition to that, the fiber is also exported to the United States, Guatemala, South Africa, Kenya and many other countries. Among these customers, however, Japan and India are by far the largest, together sharing approximately one half of the total exports for any given year. Table 7 below shows the quantities exported to some individual countries between 1966 - 1969.

TABLE 7

Thailand's Jute & Kenaf Exports, 1966 — 1969

(by Countries)

Countries	1966	1967	1968	1969
		(1,000 Metric Tons)		
Japan	64.89	91.28	79.06	73.38
India	272.29	51.64	20.67	51.25
Belgium	22.62	27.90	35.94	14.60
Italy	20.22	19.90	15.94	10.29
France	11.25	15.90	19.14	12.53
Germany (W.)	10.28	10.62	12.38	7.44
U.K.	8.39	14.24	19.27	13.19
Portugal	8.04	10.34	13.43	6.81
U.S.A.	6.20	10.29	8.50	8.83
Spain	13.33	7.89	2.56	13.70

Source: Department of Customs.

The aggregate demand for Thai kenaf reflects primarily supply and demand conditions on the international markets. Therefore, changes in prices in London market are reflected in generally similar changes in farm prices in Thailand. Table 8 demonstrates the extent of price fluctuations on the monthly basis for Thai kenaf in London market between 1966 - 1970.

The prices of Thai kenaf as quoted above are also low when compared with those of Pakistan jute; on the average, Pakistan jute enjoys prices which are well above these for Grade A Thai kenaf, in addition to being more stable. Table 9 gives the representative export prices of Pakistan jute in the seasons 1968/69 to 1970/71.

Conclusions

The above discussion has revealed some basic problems inherent in the development and trade of the kenaf fiber industry in Thailand. These factors apparently have acted as the major obstacles to further development of the Industry and continued trade expansion.

TABLE 8

Average Monthly Prices of Thai Kenaf in London Market 1966-1970

	Jan.	Feb.	March	April	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
	(in £ sterling) All prices are per long ton (C&F European Main Ports)											
Grade A												
1966	90.10	92.0	96.11	98.0	101.0	98.10	94.10	85.0	75.0	73.10	76.0	79.1
1967	81.0	79.0	80.0	70.0	67.0	65.10	63.10	62.10	62.0	60.5	65.10	69.1
1968	65.0	59.10	58.10	60.10	61.0	—	—	—	—	—	—	—
1969	101.0	98.0	93.0	88.0	84.0	77.0	76.0	73.0	68.10	65.10	71.10	77.
1970	79½	85	79½	79½	79½	84½	83	80	78	83½	91½	93½
Grade B												
1966	82	83	89½	92	95½	94½	90½	81	70	67	71	73
1967	74	72½	68	63	59½	57½	55	57	57	54½	56½	57½
1968	51½	47½	46	48	49	—	—	—	—	—	—	—
1969	94½	91½	87½	82½	78	71½	71	68	63	59½	65½	71½
1970	73	79½	76	75	74½	80	78½	75	73	78	87	89½
Grade C												
1966	75	75½	76½	78½	81½	81	77½	70½	61	57½	62½	64½
1967	65	63½	59½	53½	48½	46½	45½	46½	48	44½	45½	47
1968	41	37½	36	37½	41	—	—	—	—	—	—	—
1969	84	83	79½	73½	68	62½	64	62	57	52½	54½	64½
1970	65½	71	67½	67	65	72	71	68	65½	71	82½	83

Source: Thai Jute Association.

TABLE 9

Representative Export Prices of Pakistan Jute 1968/69 – 1970/71

	1968/69	1969/70	1970/71
		(prices in £ per long ton)	
July	109	113	115
August	114	113	116
September	114	113	113
October	127	113	113
November	130	115	113
December	130	115	113
July-December Average	121	114	114
January	130	115	113
February	130	115	
March	130	116	
April	130	118	
May	127	118	
June	122	120	
January-June Average	128	117	
Seasonal Average	124.5	115.5	

Source: FAO (OCP: JU/CC 71/3).

In concluding the discussion a few points deserve special emphasis on the ground of their relevance to future policy consideration.

1. Despite its gloomy future in view of the increasing competition from synthetic products and other substitutes as well as the extremely unstable prices in the international markets, kenaf remains a product of considerable significance to the economy of Thailand. Its actual and potential ability to generate income and employment and to create an important source of foreign exchange earnings cannot be overestimated. For this reason, careful attention should be given to the development of this industry, and such an attention must cover all stages of activities with a view to identifying specific problems and overcoming them promptly with pragmatic measures.

2. In general, the problems of the kenaf fiber industry centre on an extreme instibility of the price originating from demand and supply conditions in the world market. As it has only a relatively small share in the total world supply of coarse fibers, it is not possible for Thailand to exercise

any effective control of the price level. Given that fluctuations in world prices will continue, Thailand should attempt to neutralize their effects on domestic supply conditions with the following measures:

2.1 The Government to guarantee a minimum price for the Grade A fiber provided that conditions on quality and the delivery deadline of the products for export are met.

2.2 The Government to arrange on behalf of the local jute mills, for forward purchases of the fiber at the quantity and grades as required by the mills.

3. It must be recognized that one of the factors which contribute to price fluctuation as well as low prices for the kenaf fiber in the international market is the poor and unreliable quality of the product itself. A solution to this problem which would help raise and stabilize prices would be for the Government in cooperation with the Thai Jute Association to undertake to increase the effectiveness of the quality grading system which extends backwards to the baling operations in the provinces.

4. For the development of the industry in the long run, there is need for serious investgetion new uses of kenaf. Having regard to the reality of the threat from synthetic products and other substitutes, further delay in the discovery of significant new uses will tend to aggravate the situation of low and unstable prices in the international markets. In Thailand, research work has been carried out on the use of kenaf fiber and of the woody stems for the manufacture of pulp for paper. Much of the future prospects of the kenaf industry depends, as far as we can see, a great deal upon the success of pioneering research projects such as this.*

*As Mr. N. Pombhejara was unable to attend the Conference, there was no specific discussion of his paper.

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Trade in Manufactured Products (I)

HONG KONG TEXTILE EXPORTS
A CASE STUDY OF VOLUNTARY RESTRAINTS*

by

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Voluntary export restraints (VER), as used in this paper, take the form of a commodity trade agreement between an exporting and an importing country.[1] VER can be construed as voluntary only in the sense that any such agreement reached must have the consent of the exporting country regarding the restrictions to be imposed on its exports. It can thus be regarded as a strategic move on the part of the exporting country in order to have some say at the bargaining table, when unilateral action by the importing country appears to be inevitable.

As long as the exporting country has some leverage in the negotiations regarding the specifics of the restraints, it is most probable that the terms of the agreement tend to be less restrictive from the standpoint of the export industry concerned. For example, the allowance for the initial quota and its subsequent increases can be more liberal. In addition, the categorization can be broader so as to shape the growth pattern of the export industry in accordance with the prevailing comparative advantage or priority scale.

Owing to Hong Kong's prominence in the VER scheme regarding textiles, this paper intends to look closely into the various aspects of this scheme as exemplified in the textile exports of Hong Kong. More specifically, it (1) examines the trade restraint agreements reached between Hong Kong and various high-wage countries; (2) scans the *modus operandi* of the system of VER in Hong Kong; (3) analyses the effects of VER on textile exports in terms of growth, product diversification and sophistication, and the direction of trade; and (4) appraises its impact on the industrial structure. Finally, on the basis of Hong Kong's experience in implementing the VER system, some policy suggestions are made.

Trade Restraint Agreements

Notwithstanding the stipulation in Article XI of GATT that no quantitative restrictions were allowed, the United Kingdom had Hong Kong agree in February 1959 to a "voluntary" restraint of its cotton textile exports under the Lancashire Pact. This Pact, in fact, can be considered as the forerunner of the Geneva Short-Term Cotton Textiles Agreement of 1961 and the Long-Term Agreement of 1962.

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*This paper will be presented at the 4th Pacific Trade and Development Conference to be held in Ottawa, Canada, October 7-10, 1971. I am grateful to Edward Chen for his assistance.

[1] Thus this paper is not concerned with, for example, the restraints self-imposed by export cartels in Japan. Nor is it concerned with the recent restraints of textile exports to USA self-imposed by Japan and by Hong Kong, which were however at considerable variance with the subsequent agreements signed in October 1971.

That GATT considered quantitative restrictions on the export of cotton textiles[2] as an exceptional case can be attributed to their importance in the trade between low-wage and high-wage countries, together with the dimension of industrial readjustment problems they are likely to pose in the high-wage countries. Thus in July 1961 under the auspices of GATT, negotiations were under way towards a short-term arrangement on cotton textiles and the setting up of a Cotton Textiles Committee. This Committee drew up the Long-Term Arrangement regarding International Trade in Cotton Textiles, which went into effect on October 1, 1962, for an initial period of five years and with two extensions has remained in force.

The document provided the basis for Hong Kong's trade restraint agreements with the following countries: USA, Canada, EEC members, Norway, Sweden and Australia. Accordingly all these agreements have been reached largely in compliance with the stipulations of the Long-Term Arrangement. The initial ceiling figures are calculated on the basis of Hong Kong's actual exports to these countries during the 12-month period ending three months prior to the request for export restraint. In all the agreements, allowance is made for annual increases in ceiling figures. In almost all the agreements,[3] market disruption constitutes the *raison d'être* for requesting consultation. All the agreements allow for the swing scheme[4] and provide for periodic reviews. They also permit carry-over of unused quota to the following year and over-fulfillment in anticipation of under-fulfillment in the ensuing year. On the other hand, the trade restraint agreements with Norway and Sweden have departed from the specification of the Long-Term Arrangement in their inclusion of synthetic products.[5]

It may be of interest to contrast these agreements with the Lancashire Pact which lies outside the jurisdiction of the Long-Term Agreement. They differ essentially in the allowance for annual increases of ceiling figures. While the Lancashire Pact (1959-1965) made no stipulation at all for annual increases of ceiling figures,[6] an allowance of annual growth varying from 5-10 per cent is stipulated in Hong Kong's other trade restraint agreements. Even after UK replaced the Lancashire Pact with the Global Quota Scheme in 1966,[7] the growth allowance amounted to a mere gesture (1 per cent per year).

The trend towards more elaborate categorization in trade restraint agreements is worth noting. In the trade restraint agreements (i.e. the Lancashire Pact and the Global Scheme) between Honk Kong and UK, for example, the number of categories increased from four in 1959 to thirty-four in 1964 when the Categorization Arrangement was arrived at. Similarly the trade restraint agreement between Hong Kong and USA started with eight

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[2] Cotton textiles, as defined in the Long-Term Arrangement, include yarn, piece-goods, made-up articles, garments and other textile manufactured products, in which cotton represents more than 50% (by weight) of the fibre content, with the exception of handloom fibre of the cottage industry.

[3] In the agreement with Norway, no reference to market disruption has been made.

[4] Where restraint is exercised for more than one product, the agreed level for any product may be exceeded by 5 per cent provided that the total exports subject to restraint do not exceed the aggregate level.

[5] K. Sung and P. H. M. Jones (ed.), *Asian Textile Survey: 1969-1970*, Hong Kong, 1970, p. 98.

[6] The increase of ceiling figure in 1961 should not be construed as growth allowance, as it was the result of a new agreement.

[7] The period covered under the Global Quota Scheme was initially from 1966-1970. It was extended to the end of 1971 when it will be replaced by tariffs.

categories in 1961 and has increased to sixty-four categories since 1965. In this trend towards more elaborate categorization, UK and USA have taken the lead. Hong Kong's agreements with them now cover practically all categories of cotton textiles from yarn and cloth to made-up articles and garments, while the coverage of Hong Kong's agreements with the other countries has not yet extended beyond shirts and a few items of made-up articles.

System of Restraints

The Department of Commerce and Industry of the Hong Kong Government is responsible for all matters pertaining to trade restraint agreements. Externally it represents Hong Kong in negotiations and consultations with high-wage cotton textile importing countries. Internally it is the decision-making body in respect of quota allocation among textile manufacturers and exporters. In order to better represent the interests of Hong Kong's textile industry, a Cotton Advisory Board was set up in 1961 to advise the Director of Commerce and Industry especially on the conduct of negotiations and the implementation of trade restraint agreements. Its scope was widened in 1969 to cover garment producers. Concomitantly its name was changed to the Textiles Advisory Board (TAB).

The present membership of TAB consists of the Director of Commerce and Industry as Chairman, thirteen prominent producers from the various sectors of the textile industry,[8] two exporters of textiles, and four noted figures of the Hong Kong business community. All the members are nominated by the Director of Commerce and Industry to serve as individuals rather than representatives of their firms.

Since the primary function of TAB, as pointed out above, is to advise the Director of Commerce and Industry with respect to trade restraint agreements, the Director upon receipt of a request for consultation from an importing country normally calls a Board meeting to seek its advice. During negotiations taking place either in Hong Kong or abroad, while the Department of Commerce and Industry represents Hong Kong at the conference table, some TAB members (particularly those from the textile industry) are asked to serve as technical advisors. Although in this capacity they do not actually take part in any negotiation sessions, their views can well guide the outcome of the negotiations.

The core of the system of restraints lies in the allocation of quotas among manufacturers and exporters.[9] Whereas the final decision on quota allocations rests with the Director of Commerce and Industry, he normally consults TAB on the criteria governing quota allocations. It is these criteria which will affect the development of the textile industry in the long run.

The over-riding principle governing quota allocation is to maximize the utilization of the ceiling figures of a given importing country. With this principle as the major consideration, a few criteria have been adopted in Hong Kong with respect to quota allocation. By far the most important criterion is past performance which constitutes the basis of the Quota Control Scheme.[10] Such a criterion though intended to achieve maximum utilisation

[8] Four from garment, three weaving, three spinning, two knitting and one finishing.
[9] The exporters will, in turn, allocate their quotas among the producers working through them.
[10] Under this scheme, firms with 95 per cent fulfillment of the past year's quotas are allocated the same quotas plus a 1 per cent increase; firms fulfilling 50-95 per cent of the past year's quotas are given the same quotas; and for firms fulfilling less than 50 per cent of the past year's quota, no allocation is made.

of given ceiling figures tends to favour the established firms and makes the entry of new firms more difficult. The economic rationale behind this criterion is that the established firms have attained a more efficient scale of production. Moreover, there are two practical considerations: first, these firms have already established links with foreign buyers and second, it is administratively simpler to base allocations on past export records.

For the benefit of those textile producers who cannot qualify on the ground of past performance, the criterion of high Hong Kong cost content has been adopted. These producers accordingly can qualify for quota allocation if their products meet the minimum requirement of HK$2.10 worth of Hong Kong content per square yard of cotton fabrics equivalent. As they are competing for the unfilled quotas under the Quota Control Scheme,[11] the higher the Hong Kong cost content in their products, the better their chances of obtaining quota allocation.

In the event that some producers to whom quotas have been allocated for one reason or another[12] cannot make full use of their quotas in the given period, such unused quotas[13] can then be re-allocated on the basis of "first come first serve" under the Special Shipment Scheme. However, this scheme also requires that the minimum Hong Kong cost content is satisfied.

Since the principle underlying the system of restraints in Hong Kong is to maximize the utilization of the ceiling figures, it would be of interest to see the extent to which the quotas have actually been utilized. The extent of utilization should constitute a basis for appraising the operation of the system of restraints. Data on the degree to which the VER quotas have been fulfilled are presented in Table 1. On the whole, quota fulfillment has been highly satisfactory. The fulfillment records are particularly good in the three major markets for Hong Kong cotton textile exports (USA, UK and West Germany). For the period 1962-1969, quota fulfillment came to 99.9 per cent for USA, 96.8 per cent for UK and 95.7 per cent for West Germany.

Inasmuch as the system of restraints in Hong Kong appears to favour the large firm, it would also be of interest to find out whether there has been any indication of increasing concentration in the textile industry. For this purpose, changes in the size distribution of firms during 1962-1970 have been examined. The prevailing size of firm in the spinning and garment sectors, according to the Florence criteria, shows no noticeable change.[14] For the spinning sector where data on production capacity of individual firms are obtainable, the traditional "big four" concentration ratio has been calculated. Here again, the concentration ratio shows no increase over time.[15] It therefore appears that there is no tendency towards higher concentration

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[11] The unfilled quotas consist of those previously allocated to firms which fulfilled less than 50 per cent of their allocations, and the excess of the increase in ceiling figures allowed in trade restraint agreements over the 1 per cent increase allowed in the Quota Control Scheme.

[12] Such as unforeseen cancellations of orders, or an unexpected rise in production cost which makes it unprofitable to fulfill the quota.

[13] Except the portion of the unused quotas which has been sold to interested producers within a specified period of time and with the approval of the Department of Commerce and Industry.

[14] For data showing changes in the size distribution of firms from 1962-1970, see Table A in the Appendix. For the Florence criteria, see P.S. Florence, *Logic of British and American Industry*, London, 1961, p. 27.

[15] See Table B in the Appendix.

TABLE 1

Quota Utilization, 1962/63–1968/69
(per cent)

Year* / Country	1962-63	1963-64	1964-65	1965-66	1966-67	1967-68	1968-69
U.S.A.	98.3	96.9	99.5	108.2	94.3	102.2	100.4
U.K.	103.0	99.5	99.6	97.8	89.5	92.9	95.0
West Germany	98.8	88.3	89.3	100.0	93.7	98.7	100.9
Canada	86.3	78.9	120.9	90.1	76.3	71.8	77.1
Sweden	—	—	—	—	—	—	83.6
Norway	—	—	—	—	—	—	83.0
Benelux	—	—	—	84.2	80.7	67.4	79.5

*Quota year is from October 1 to September 30.

Source: Based on data given in Director of Commerce and Industry, *Annual Departmental Reports, 1969-70*, Hong Kong: Government Printer, 1970, pp. 96-98.

in the spinning and garment sectors. In the weaving sector, however, some tendency towards higher concentration has been detected, as the percentage of employment in firms in the top two classes employing 500 workers or more has increased from 1962-1970.[16]

Growth of Textile Exports

The instituting of VER and the operational set-up it called for have inevitably affected the growth and the pattern of textile exports. One of the noticeable effects was the slowing down of the growth rate in the exports of yarn, fabrics and made-up articles. To show this effect, two time periods are selected for comparison: 1956-1961 and 1962-1970.[17] As can be seen from Column 2 of Table 2, the annual growth rates of the exports of yarn, fabrics and made-up articles averages 19.3 per cent during 1956-1961, but merely 7.8 per cent during 1962-1970. The dwindling of growth rates resulted in the declining relative importance of these exports in the overall (domestic) exports of Hong Kong. Their percentage share decreased from 22.8 in1961 to 10.3 in 1970 (See Column 3 of Table 2).

The decline in the rate of export growth was not accompanied by a rise in domestic consumption, as the rate of increase in output concomitantly slowed down. Table 3 shows that the annual average growth rate of the output of yarn and that of fabrics and made-up articles declined from 16.0 and 20.9 per cent during 1956-1961 to 7.0 and 5.6 per cent respectively during 1962-1970.

The garment sector, on the other hand, was not as much affected by VER. In fact, the annual average growth rate of its exports increased from 18.8 per cent during 1956-1961 to 19.9 per cent during 1962-1970 (See Column 2 of Table 4). Concomitantly its percentage share in overall (domestic) exports rose from 34.8 per cent in 1959 to 35.1 in 1970 (See Column 3 of Table 4). The performance of garment exports reflects the capability of the garment sector in adapting itself to the new situation brought about by VER. From this contrast, however, one should not hastily draw the inference that the entrepreneurs in the spinning and weaving sectors are less capable of adjusting to the changing situation, for they are confronted with specific problems and difficulties which do not arise in the garment sector.[18]

Diversification of Products

In addition to slowing down the growth rate of cotton textile exports, VER has perhaps hastened to some extent the shift from cotton to non-cotton textile exports, particularly the exports of garments. For the period from 1962-1970 there was, on the basis of value data, a gradual decline in the relative importance of cotton garments and a rapid rise in that of non-cotton garments. Data on export value, however, may not reflect accurately changes in physical quantity because of price-change differentials and the elasticity of demand for the two categories of garments. It is, therefore, necessary to see the relative changes in their export quantities.

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[16] See Table A in the Appendix.

[17] This division of time periods coincides with the Geneva Arrangements Regarding International Trade in Cotton Textiles. Such a division understandably overlooks the early effects of the Lancashire Pact.

[18] The adjusting process will be discussed in the ensuing section on product diversification and sophistication.

TABLE 2

Exports of Textile Yarn, Fabrics and Made-up Articles, 1956-70

Year	Export Value (HK$ million)	Increase over Preceding Year (per cent)	Share in Total Domestic Exports (per cent)
	(1)	(2)	(3)
1956	295.9		
1957	367.2	24.1	*
1958	351.3	-4.3	*
1959	413.9	17.8	18.1
1960	554.2	33.9	19.3
1961	669.0	20.7	22.8
1956-61 (average)		19.3	
1962	590.3	-11.8	17.8
1963	648.3	9.8	16.9
1964	706.7	9.0	16.0
1965	834.5	18.1	16.6
1966	921.3	10.4	16.1
1967	935.5	1.6	14.0
1968	1,035.1	10.6	12.3
1969	1,126.2	8.8	10.7
1970	1,276.7	13.4	10.3
1962-70 (average)		7.8	

*It is not possible to calculate this share prior to 1959, as export statistics were not classified separately as re-exports and domestic exports. While the negligible re-exports of textile products permit us to treat given data as a close approximation of domestic exports; the importance of re-export trade as a whole prevents a similar treatment for overall domestic exports.

Source: *Hong Kong Trade Statistics.*

TABLE 3

Production of Textile Yarn, Fabrics and Made-up Articles, 1956-1970

Year	Yarn Output (lb.)	Annual Growth Rate (per cent)	Output of Fabrics and Made-up Articles ('000 sq. yd.)	Annual Growth Rate (per cent)
1956	104,857		195,144	
1957	112,434	7.2	264,481	35.5
1958	129,571	15.2	279,759	5.8
1959	143,135	10.5	365,843	30.8
1960	177,464	24.0	467,964	27.9
1961	218,578	23.2	488,511	4.4
1956-61 (average)		16.0		20.9
1962	243,809	11.5	512,118	4.8
1963	252,374	3.5	568,146	10.9
1964	274,140	8.6	577,748	1.7
1965	308,421	12.5	646,040	11.8
1966	321,567	4.3	682,612	5.7
1967	332,811	3.5	738,025	8.1
1968	365,464	9.8	798,550	8.2
1969	371,203	1.6	782,704	-2.0
1970	398,130	7.3	794,821	1.6
1962-70 (average)		7.0		5.6

Source: Census and Statistics Department, *Hong Kong Monthly Digest of Statistics*, Hong Kong: Government Printer, March, 1971.

TABLE 4

Exports of Clothing, 1956-1970

Year	Export Value (HK$ million)	Increase over Preceding Year (per cent)	Share in Total Domestic Exports (per cent)
	(1)	(2)	(3)
1956	398.4		
1957	437.0	9.7	*
1958	520.4	19.1	*
1959	793.2	52.4	34.8
1960	1,010.4	27.4	35.2
1961	862.1	-14.5**	29.3
1956-61 (average)		18.8	
1962	1,147.4	33.1	34.6
1963	1,382.9	20.5	36.1
1964	1,619.7	17.1	36.6
1965	1,772.6	9.4	35.3
1966	2,035.5	14.8	35.5
1967	2,316.6	13.8	34.6
1968	3,013.9	30.1	35.8
1969	3,827.6	27.0	36.4
1970	4,336.6	13.3	35.1
1962-70 (average)		19.9	

*It is not possible to calculate this share prior to 1959, as export statistics were not classified separately as re-exports and domestic exports. While the negligible re-exports of textile products permit us to treat given data as a close approximation of domestic exports; the importance of re-export trade as a whole prevents a similar treatment for overall domestic exports.

**This drastic reduction was attributable primarily to the over-stocking of Hong Kong clothing during 1959-1960 in the U.S. market in anticipation of imposition of restrictions following the UK practice.

Source: *Hong Kong Trade Statistics.*

For this purpose, the ratios of cotton to non-cotton garment exports have been worked out on the basis of export quantities for the same period. Consistent with the findings based on value data, these ratios are also found to be declining. As can be seen from Table 5, the ratio of cotton to non-cotton shirts and trousers dwindled from 12.4 in 1962 to 1.4 in 1970. Correspondingly the percentage share of cotton shirts and trousers on value basis dropped from 25.9 in 1962 to 13.0 in 1970 whereas that of non-cotton shirts and trousers rose from 3.5 in 1962 to 13.1 in 1970.

Similar shifts are discernible in both weaving and spinning. On the basis of export quantities, percentage shares of cotton and non-cotton fabrics and made-up articles in the overall exports of the weaving sector have been calculated and are presented in Table 6. While the share of cotton fabrics and made-up articles decreased from 98.5 in 1962 to 91.3 in 1970, the non-cotton share increased from 0.6 in 1962 to 7.5 in 1970.[19]

The change-over from cotton to non-cotton yarn exports involved woolen as well as synthetic yarn. As shown in Table 7, the percentage share of cotton yarn in the overall yarn exports (also based on physical quantities) dropped from 97.1 in 1962 to 81.7 in 1970. On the other hand, the share of synthetic yarn rose from 0.5 in 1962 to 14.0 in 1970, and the corresponding increase for woolen yarn was from 0.2 to 4.1.

The findings in respect of the shift from cotton to non-cotton textile exports are consistent with the earlier findings on the relative growth of the garment sector on the one hand, and spinning and weaving sectors on the other in that both in terms of the rate of growth in exports and of the export ratio of cotton to non-cotton products, garment producers appear to have been more adaptable to the new situation brought about by VER.

This observation, however, has not taken into account the fact that spinners and weavers are confronted with specific difficulties not shared by the garment producers. One such difficulty is that the shift to synthetic yarn and fabrics requires substantial re-investment on the part of the spinners and weavers, inasmuch as the machinery and equipment used in manufacturing cotton yarn and fabrics are unsuitable for synthetic products. Such a heavy investment necessitated by the shift to synthetics tends to inhibit the rate of technology diffusion in the spinning and weaving sectors.[20] In the garment sector, on the other hand, the existing machinery and equipment can be used for processing synthetic inputs with minor modifications. Thus no sizeable re-investment in connection with the shift to synthetic products is called for in the garment sector.

Another difficulty is the lack of supporting industries in Hong Kong for the development of synthetic spinning and weaving. In the absence of chemical industries, Hong Kong has to rely entirely on overseas supply of synthetic fibres. The situation was further complicated by the cartelization of synthetic fibre in international trade, under which Hong Kong had to accept monopoly prices from the designated source of supply. Consequently the development of synthetic spinning and weaving was delayed until the mid-1960s when the enforcement of the cartel agreement was sufficiently relaxed so that Japan was able to supply Hong Kong with the much needed raw material at substantially lower prices.

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[19] The percentage shares of other non-cotton fabrics and made-up articles including notably silk and woolen remained more or less unchanged.

[20] See E. Mansfield, *Industrial Research and Technological Change*, New York, 1969, p. 136-144.

TABLE 5

Proportions of Cotton and Non-cotton Shirts and Trousers to Overall Clothing Exports, 1962, 1964 and 1966-1970

Year	Proportion of Cotton Shirts and Trousers (per cent)	Proportion of Non-cotton Shirts and Trousers (per cent)	Export Ratio of Cotton to Non-cotton Shirts and Trousers
	(1)	(2)	(3)
1962	25.9	3.5	12.4
1964	23.8	4.1	9.8
1966	20.0	7.3	4.2
1967	18.8	9.9	2.6
1968	19.1	9.6	2.8
1969	15.5	8.4	2.4
1970	13.0	13.1	1.4

Note: Columns (1) and (2) are based on value data and column (3) on physical quantities. Hence the export ratios are independent of the percentage figures given in columns (1) and (2).

Source: Based on data given in *Hong Kong Trade Statistics.*

TABLE 6

Relative Importance of Cotton and Non-cotton Products in the Exports of Textile Fabrics and Made-up Articles, 1962, 1964 and 1966-1970
(per cent)

Year	Cotton Fabrics and Made-up Articles	Non-cotton Fabrics and Made-up Articles
1962	98.5	0.6
1964	98.3	0.7
1966	94.3	4.8
1967	95.8	3.1
1968	95.9	2.8
1969	93.4	5.2
1970	91.3	7.5

Source: Based on export data in physical quantities given in *Hong Kong Trade Statistics.*

TABLE 7

Relative Importance of Cotton, Synthetic and Woolen Yarn in Total Yarn Exports, 1962, 1964 and 1966-1970
(per cent)

Year	Cotton Yarn	Synthetic Yarn	Woolen Yarn
1962	97.1	0.5	0.2
1964	97.8	1.7	0.6
1966	95.0	3.5	1.3
1967	92.4	5.6	1.9
1968	90.2	6.2	3.4
1969	85.0	9.2	5.7
1970	81.7	14.0	4.1

Source: Based on export data in physical quantities given in *Hong Kong Trade Statistics.*

TABLE 8

Average Export Prices of Cotton Fabrics and Cotton Shirts, 1962, 1964 and 1966-1970

Year	Cotton Fabrics (HK$/sq. yd.)	Cotton Shirts (HK$/dozen)
1962	1.05	*
1964	1.18	23.73
1966	1.13	26.08
1967	1.15	27.56
1968	1.23	32.76
1969	1.29	38.15
1970	1.31	44.74

*The classification of shirts in 1962 was different and not comparable.

Source: Based on data given in *Hong Kong Trade Statistics.*

Product Sophistication

With cotton textile exports, there has been a shift from products with less processing and sophistication to those with more. Such a shift can be attributed partly to the fact that VER is expressed in quantity rather than value terms. Moreover, it is re-enforced by the above-mentioned High Hong Kong Cost Content Scheme. The shift from less to more processing can be seen from the faster growth of non-grey yarn exports relative to grey yarn exports. The latter increased from HK$85.2 million in 1964 to $92.0 million in 1970, whereas the former from $1.7 million in 1964 to $9.4 million in 1970.[21]

There is also a shift from less to more sophisticated products in textile exports. Such a shift can be detected, to some extent, in the changing unit value of weaving and garment exports under VER. The average export price of cotton fabrics per square yard amounted to HK$1.05 in 1962 and HK$1.31 in 1970. Similarly the average export price of cotton shirts increased from HK$23.73 per dozen in 1962 to HK$44.74 per dozen in 1970[22] (see Table 8).

Direction of Trade

With the instituting of VER, one would have expected some trade diversion from VER countries[23] to non-VER countries. To determine whether such a change has taken place, it is necessary to classify export data into these two groups of countries. The percentage distribution of cotton textile exports between these two groups on the basis of data in both physical quantities and value terms is given in Table 9. In the case of yarn and fabrics for which quantity data are not available, value data constitute the sole basis.

Contrary to expectation, the percentage distribution for all categories of cotton textile exports except one is quite constant over time, as no statistically significant trend lines can be fitted to the changes over time for the period 1964-1970. The only evidence of trade diversion is found in the exports of cotton dress shirts.[24] In this case, however, trade diversion turns out to be in favour of VER countries.

For this unexpected export behaviour, some explanations are called for. Since the bulk of Hong Kong's exports has always been going to VER countries, there have developed some built-in institutional factors governing the direction of trade. Moreover, these factors tend to have cumulative effects over time.

Secondly, the line dividing VER and non-VER countries also divides the developing and developed economies, and the two groups of countries have divergent consumption patterns. Hong Kong's exports to the developed countries consist preponderantly of higher-priced and more sophisticated commodities. As an illustration, let us refer to Table 9 which shows that the market share of VER countries is invariably larger in value terms than in physical quantities. Any trade diversion in favour of non-VER countries

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[21] *Hong Kong Trade Statistics.*

[22] Price increases not reflecting higher sophistication are believed to be negligible, in view of the keen competition and productivity increases.

[23] The term "VER countries" refers to those countries with which Hong Kong has VER arrangements, viz., UK, USA, Canada, West Germany, the Netherlands, Belgium, Luxemburg, France, Italy, Sweden, Norway and Australia.

[24] The trend line in this case is positive and statistically significant at the 0.01 level.

TABLE 9

Percentage Share of Cotton Textile Exports to Quota Countries

Item		1964	1965	1966	1967	1968	1969	1970
Shirts, not knitted or crocheted	Q	84.4	81.9	81.2	81.0	82.8	81.2	80.6
	V	88.1	84.2	84.0	82.4	86.4	85.7	87.1
Dress shirts, not knitted or crocheted	Q	76.1	79.0	79.9	81.0	84.1	86.5	84.6
	V	77.0	81.0	82.4	84.0	85.6	88.6	87.6
Shirts, knitted or crocheted	Q	79.1	75.8	77.4	78.6	82.6	83.9	81.1
	V	83.4	82.0	83.5	86.9	88.0	86.4	85.3
Slacks, shorts, jeans and trousers	Q	84.6	84.4	82.7	82.7	85.8	84.9	81.5
	V	90.1	90.2	87.9	87.4	89.2	88.4	84.5
Cotton Textile Yarn	V	24.5	24.1	34.1	36.7	33.9	30.1	27.4
Cotton Fabrics	V	65.2	67.7	65.8	66.4	69.9	67.1	61.6

Q, based on physical quantities.
V, based on export value.

Source: Based on data given in *Hong Kong Trade Statistics.*

would entail a change in the industrial output structure contrary to the very process of development.

Thirdly, in the developing countries the purchasing power is generally limited. Their capacity to import varies according to foreign exchange earnings and foreign exchange availability. Thus Hong Kong's textile exports to Ceylon, for example, fluctuate considerably from year to year. In view of this uncertainty and the limited effective demand, Hong Kong entrepreneurs perhaps consider it inadvisable to shift their focus to the developing countries.

Finally, in their industrialization scheme most developing countries start with cotton textiles. Thus this industry is among the first to be protected. Consequently many non-VER countries have imposed tariffs on textile imports.

Changes in Industrial Structure

A significant development in Hong Kong's manufacture exports in response to VER is, perhaps, the pursuance of new lines of manufacture outside the textile field. The Hong Kong economy being export-oriented cannot afford to rely heavily on any single industry. This is particularly true because of its free trade policy. Thus the economy's need for diversification is painfully brought to the fore by the instituting of VER. This exogenous shock has undoubtedly hastened the diversification process.

Changes in the relative importance of the exports of various industries from 1959-1970 are shown in Table 10. The rapidly rising relative importance of electronics and wigs is particularly noteworthy. In 1960, there was hardly any electronics industry in Hong Kong. By 1970, however, this new industry accounted for 8.7 per cent of Hong Kong's overall (domestic) exports. The rise of the wig industry was even more spectacular. As late as 1964, this industry was insignificant. Within six years, it became the fourth largest export industry. In addition, the percentage share of plastic toys and dolls doubled between 1959 and 1968.

For such speedy adjustment in Hong Kong's industrial structure, credit should be given to the ingenious entrepreneurs. The ingenuity with which they responded to VER has turned a harmful exogenous force into an impetus for further development.

Concluding Remarks

The findings reveal that the system of restraints in Hong Kong has worked reasonably well in terms of (1) quota fulfillment, (2) raising the manufacture content of commodities under VER, and (3) increasing the sophistication of certain textile products. Remarkably these attainments are not accompanied by unhealthy tendency towards excess concentration.

The instituting of VER has slowed down the growth of cotton textile exports, but has probably hastened the shift from cotton to non-cotton textile exports and from products with less processing and sophistication to those with more. The development of new products and the increase in manufacture content and sophistication are the very ingredients indispensable in the process of industrial development. They are instrumental in generating income and employment and in promoting technological change. Seen in this light, perhaps VER may not have been as harmful to Hong Kong's industrial development as one would have expected.

In spite of VER, there has been no noticeable trade diversion. This can be attributed chiefly to the built-in institutional factors favouring trade

TABLE 10

Principal Manufacture Exports of Hong Kong by Industry
1959 – 1970
(HK$ million)

Year	Textiles		Plastic Flowers		Plastic Toys & Dolls		Electronics		Electrical		Metal		Footwear		Wigs	
	Value	%*	Value	%*	Value	%*	Value	%*	Value	%*	Value	%*	Value	%*	Value	%*
1959	1,207.2	52.9	62.4	2.7	89.5	3.9			35.2	1.5	135.9	6.0	109.0	4.8		
1960	1,564.6	54.6	148.6	5.2	99.7	3.5	0.3	0.01	47.0	1.6	151.5	5.3	114.5	4.0		
1961	1,531.1	52.1	171.8	5.8	113.9	3.9	12.9	0.4	60.3	2.0	154.4	5.3	103.7	3.5		
1962	1,737.7	52.4	197.1	5.9	138.4	4.2	37.1	1.1	69.3	2.1	166.0	5.0	129.5	3.9		
1963	2,031.2	53.0	216.1	5.6	170.9	4.5	71.2	1.9	81.5	2.1	176.6	4.6	146.3	3.8		
1964	2,326.4	52.5	271.0	6.1	243.0	5.5	108.1	2.4	78.2	1.8	188.3	4.3	174.6	3.9	6.0	0.1
1965	2,608.0	51.9	266.0	5.3	321.0	6.4	212.6	4.2	80.6	1.6	207.4	4.1	152.7	3.0	45.0	0.9
1966	2,956.8	51.6	258.0	4.5	385.0	6.7	359.7	6.3	116.4	1.8	230.9	4.0	184.2	3.2	71.0	1.2
1967	3,252.1	48.5	288.0	4.3	504.0	7.5	423.8	6.3	166.1	2.5	266.6	4.0	218.9	3.3	197.0	2.9
1968	4,049.0	47.7	308.0	3.6	666.0	7.9	575.2	6.8	146.8	1.7	311.3	3.8	271.4	3.2	318.0	3.8
1969	4,953.8	47.1	365.9	3.5	770.6	7.3	827.7	7.9	230.6	2.2	364.0	3.5	295.2	2.8	647.2	6.2
1970	5,613.3	45.5	416.0	3.4	871.6	7.1	1,075.0	8.7	659.0	1.8	425.8	3.5	302.3	2.5	936.7	7.6

*Percentage share in total domestic exports.

Source: *Hong Kong Trade Statistics.*

with VER countries, and the limited import capacity and protectionist policy of non-VER countries. To some extent can the lack of trade diversion be accounted for by the quantitative nature of the restraints and the allowance for regular increases in ceiling figures. Thus the export value can be increased by raising the manufacture content of the restrained commodities, by shifting to higher-priced varieties within the same category under VER, and by developing new products.

On the basis of the experience of Hong Kong, the implementation of VER needs more explicit rules and effective control by an international organization. For example, according to the Long-Term Arrangement, any request for consultation must be based on market disruption and that it must be substantiated by detailed factual statements. Granted the intrinsic difficulty in substantiating market disruption by factual statements, the degree of substantiation has been subject to a wide range of variation. Consequently it is often debased to the level of relative bargaining strength. Hong Kong unfortunately being a firm believer in free trade and therefore lacking the power of retaliation, is often at the mercy of the requesting country with superior bargaining strength. Such disparity in bargaining strength can be eliminated, to a large extent, by more explicit rules preferably with quantitative stipulations and by setting up an international organization whose sole job would be to keep the VER system under regular surveillance.

Hong Kong's experience regarding VER also suggests the need for greater flexibility in its implementation. For example, the increasing categorization of restraints tends to inhibit specialization required for attaining the optimum scale of production. Although provisions have been made for a maximum of 5 per cent "swing scheme," this is far too restrictive to permit a growth pattern compatible with comparative advantage.

VER may not be altogether an objectionable system if restraints can be confined to a limited number of broad categories with a reasonably wide range of "swing" between them and if a liberal annual growth rate can be allowed. With these constraints, perhaps VER can be expected to promote a steady and smooth growth of the textile industry without undue interference with its pattern of growth.

APPENDIX

TABLE A

Size Distribution of Firms in the Textile Industry, 1962-1970
(per cent)

Number of Workers	1962	1963	1964	1965	1966	1967	1968	1969	1970
	Spinning								
1,000 and over	59.5	54.8	55.0	49.9	56.1	56.3	62.6	56.8	60.8
500 — 999	26.6	26.1	23.4	29.6	18.7	22.4	13.3	18.6	20.6
200 — 499	11.9	17.2	20.6	19.6	24.5	20.7	21.9	22.1	16.7
100 — 199	1.3	1.8	0.6	0.6	0.0	0.0	1.9	2.1	1.1
50 — 99	0.3	0.0	0.4	0.3	0.7	0.6	0.3	0.4	0.8
1 — 49	0.4	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	Weaving								
1,000 and over	0.0	4.7	4.6	4.3	5.3	17.0	18.2	18.3	17.7
500 — 999	15.8	10.5	10.6	10.5	16.9	10.2	10.0	7.3	10.6
200 — 499	36.4	41.7	44.3	45.8	40.0	36.2	37.4	41.1	36.8
100 — 199	23.9	20.4	22.2	19.6	22.6	21.1	16.5	15.1	16.2
50 — 99	12.5	11.6	10.1	11.3	7.6	8.0	9.2	8.5	9.9
1 — 49	11.4	11.1	8.2	8.5	7.6	7.5	8.7	9.7	8.8
	Clothing								
1,000 and over	0.0	2.1	4.5	11.7	15.8	15.5	14.2	14.7	13.6
500 — 999	21.8	22.5	22.7	19.6	16.1	10.5	16.6	14.3	12.9
200 — 499	27.6	27.8	27.5	24.9	26.7	30.7	24.9	23.7	23.6
100 — 199	18.1	16.4	18.4	18.7	16.6	16.7	16.2	17.5	18.7
50 — 99	14.7	14.5	12.4	11.5	11.3	11.4	11.5	12.8	13.8
1 — 49	17.8	16.7	14.5	13.6	13.5	15.2	16.6	17.0	17.4

Source: Labour Department, *Statistics on Registered and Recorded Industrial Undertakings Classified by Industries and Number of Employees.*

APPENDIX
TABLE B

Concentration in the Spinning Sector

Year	Concentration Ratio	Size Ratio
1960	0.38	0.025
1961	0.34	0.026
1962	0.35	0.024
1963	0.34	0.025
1964	0.37	0.024
1965	0.36	0.024
1966	0.35	0.024
1967	0.34	0.024
1968	0.32	0.024
1969	0.31	0.024
1970	0.31	0.022

$$\text{Concentration Ratio} = \frac{\text{Production capacity of the 4 largest firms}}{\text{Production capacity of all firms}}$$

$$\text{Size Ratio} = \frac{\text{Production capacity of the sector excluding the 4 largest firms}}{\text{Total number of firms - 4}}$$

Source: Computed from data supplied by the Hong Kong Cotton Spinners Association.

TRADE RESTRICTIONS AND TEXTILE EXPORTS OF SINGAPORE – A CASE STUDY

by

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Introduction

Section 1 deals with the textile industry of Singapore during the period 1964-70. It is meant to serve as a perspective and background for discussion and analysis of the following two sections. The importance of the textile industry relative to Singapore's total external trade and its contribution in terms of export, value added, and employment to the total manufacturing and quarrying sector are highlighted.

Section 2 analyses the terms of the Long-Term Arrangement regarding trade in cotton textiles[1] and the impact of non-tariff restrictions on cotton textile exports from low-wage countries (including Singapore) to the United States, the United Kingdom, and Canada. An evaluation of the restrictive effects of the LTA is made.

Finally, Section 3 deals with some of the measures that could be adopted to liberalize textile trade in general and cotton textile trade in particular.

1. Singapore's Textile Industry

The establishment of a textile industry based on cotton has been the starting point in the industrialization of many of the industrially advanced countries. This development approach has also been adopted on a wide scale by many of the developing countries undertaking a program of industrialization. "In India, China, Mexico, the development of modern cotton textile industries marked the pre-take-off period."[2] The rationale of developing the textile industry as the spearhead of industrialization is that the demand for clothing as a basic need has a mass market. Secondly, the capital requirement is low, whilst its labour-absorptive power is relatively high, so that the mechanization of the spinning, weaving, and garmenting processes which were previously carried out on a cottage-scale would enable production on a large scale.

As a part of her industrialization policy, Singapore established a textile industry in the early 1960s. In fact, the textile industry was a priority program to help remedy the high level of unemployment then.

The term 'textiles' is generally taken to mean the manufacture of fabrics and garments or wearing apparel of every kind of fibre blending. In this paper, the term is restricted to mean groups 65 and 84 of the Standard International Trade Classification (SITC). Group 65 comprises textile yarn, fabrics, and made-up articles and related products, except clothing; Group 84 is made up of clothing or wearing apparel.

It is to be noted that no attempt is made to distinguish between cotton and non-cotton textile trade in Section 1 simply because no breakdown data are published in Singapore.

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[1] Hereafter referred to as the LTA.
[2] W. W. Rostow, *Process of Economic Growth*, Oxford (1960), p. 300.

The period of study of the textile industry as defined above is limited to 1964-70, basically because the industry (in the modern sense of assembly-line factories producing for export as well as for import-substitution) only began in the early 1960s. The year 1964 was chosen as the base year to enable us to analyze the effects on Singapore's textile exports arising from the imposition of quotas by the United Kingdom, the United States, and Canada. As a first approximation of the importance of the textile industry in Singapore, we could consider Table 1, where a comparison is made between the textile trade and the total external trade of Singapore from 1964 to 1970. The outstanding feature of the textile trade is the widening gap between textile imports and textile exports. Table 1a sets out the value of textile exports as a percentage of total exports, whilst Table 1b shows the annual percentage growth in the value of textile imports and exports.

This growing deficit in the textile trade of Singapore could be attributed to two reasons: (i) on the export side, the growth of textile exports was stunted by the LTA and the various bilateral textile trade agreements arising therefrom (this will be discussed in more detail in Section 2); (ii) on the imports side, the rising home or domestic consumption of textiles. This could be verified from Table 2, which shows that retained imports in 1969 was about four-fold that of 1964. It may be argued that the rise in retained imports of textiles results more from the retention of imported textile fabrics for use in the local textile industry rather than from the retention of imported textile for final consumption. This line of argument is quite consistent with the fact that the first and only fully-integrated textile mill was established in Singapore in 1968. Therefore the bulk of intermediate inputs for the garmenting factories must have come from imports. Official statistics show that the total value of imports of Group 65 rose from about $250 million in 1964 to $810 million in 1970. Imports of Group 84, however, fell from about $88 million in 1964 to approximately $71 million in 1970.

Another relevant feature of the trade in textiles in Singapore is the indications of a change in the direction of exports. Table 3 sets out the principal countries with which Singapore imports and exports textile goods in 1964 and 1970. Table 3a shows that, although textile imports from these principal sources form about 89 percent by value of total textile imports, textile exports to these principal sources have declined from 90 percent of total textile exports to 77.7 percent in 1970. This could bear evidence to the drive by local exporters to diversity their markets, mainly due to the now-restricted access of the traditional markets in the United Kingdom, United States, Canada, and other developed countries that have imposed import quotas.

A better perspective of the textile industry may be provided if one looks at the importance of this industry vis-à-vis the total manufacturing and quarrying sector in Singapore. Although Singapore has for a long period of its economic history been regarded as an entrepot port, and re-exports of goods and services have played an important role in her over-all development, this view of things must be changed in the light of the government's increasing emphasis on further economic development through industrialization.

The number of establishments in the domestic textile industry, as seen in Table 4, is over-valued in 1964 and 1965 because of the non-exclusion of footwear manufacturing establishments. In 1966, the number stood at 99 establishments in production. The small increase over the previous year could be indicative of the general uncertainties with the United States and U.K. attitudes on the imposition of quota restrictions: 1967 was a year of

'recession' for the textile industry in the sense of the adverse impact of the quota restrictions placed by the United Kingdom and United States. However, the industry recovered and recorded a 57 percent increase in the number of establishments in 1968. The increase in the following year was by nine establishments, but the number of establishments in shirt manufacturing decreased by six. This could have resulted from the Canadian imposition of quotas on wearing apparel exports by Singapore in July, 1968.

Table 5 focusses attention on the value and direction of the domestic textile exports of Singapore. Exports of textiles to overseas countries (i.e., excluding East and West Malaysia) more than doubled in value in 1968 compared to 1967. This seems to be in line with the recovery of the industry as seen in the above paragraph.

Table 6 also records a similar picture of the textile industry in terms of the number of workers employed. The year 1968 recorded the highest percentage increase in the number of new jobs created by the industry. Apart from 1964 and 1968, employment in the textile industry forms about 11 percent of total employment in the manufacturing and quarrying sector.

Table 7 shows that value added in the textile industry hovers around 3 to 4 percent that of total value added generated by the manufacturing sector. Therefore, the industry is more important as a source of employment creation than as a source of income generation in the process of industrialization.

2. The Long-term Arrangement Regarding Trade in Cotton Textiles

The LTA was the culmination of attempts by some developed countries to find a 'solution' to the problem created by the intrusion of Japanese manufactured goods into their markets during the 1950s. In her efforts to obtain full membership of GATT (and therefore enjoyment of the most-favoured-nation tariff treatment in her international trade with GATT members), Japan employed 'voluntary restraints' on her exports of certain 'sensitive' goods like cotton textiles, china, transistor radios, and other light manufactured goods. Under this so-called orderly marketing system, Japan "agreed, subject to frequent changes, to limit to agreed amounts, to minimum prices, to minimum standards of quality, or to some combination of all these, their exports of specified goods to specified markets. In return they asked that the importing countries desist from any other discriminatory practices against these exports and in general, otherwise extend most-favoured-nation treatment to Japan."[3]

But this 'voluntary restraint' approach had several shortcomings, the most serious of which arose from the fact that it was used only by Japan. Therefore, any cutback of exports of the sensitive goods resulting from the application of export restraint was often filled by exports from other low-wage countries. Consequently, no relief was brought to domestic producers in the importing countries.

Secondly, the voluntary export restraints violated the general liberal trade commitments of all parties involved by introducing quantitative restrictions on international trade, a feature which in fact contravenes the rationale of GATT.

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[3]G. Patterson, *Discrimination in International Trade, the Policy Issues, 1945-1965*, Princeton (1966), p. 297.

The U.S. government, prodded by its interest for an expansion and liberalization of world trade and also in GATT accepting Japan as a full member, but faced with a great upsurge in protectionist sentiment in the United States itself, because of the rapid rise in U.S. imports of Japanese goods, proposed in 1959 that GATT undertake a study to find an acceptable multilateral solution to the problem of "sharp increases in imports, over a brief period of time and in a narrow range of commodities (which) can have serious economic, political and social repercussions in the importing countries."[4]

The study led to GATT adopting what Verbit termed "a definition of a new kind of economic evil, 'market disruption'."[5] Market disruptions were deemed to occur or to threaten to occur, where (i) a sharp and substantial increase or potential increase of imports of particular products from particular sources; (ii) these products are offered at prices which are substantially below those prevailing for similar goods of comparable quality in the market of the importing country; (iii) there is serious damage to domestic producers or threat thereof; (iv) the price differentials referred to in (ii) above do not arise from governmental intervention in the fixing or formation of prices or from dumping practices.[6]

Following the attempts made by various industrialized countries like the United Kingdom, the EEC countries, Austria, and Switzerland to negotiate bilateral agreements with Japan, Hong Kong, India, and Pakistan, and other low-wage producers of cotton textiles in the late 1950s and the GATT adoption of the 'market disruption' principle, the U.S. government put forth its proposal that the whole problem of trade in cotton textiles be considered in the GATT "with a view to reaching agreement on arrangements for the orderly development of the trade in such products, so as progressively to increase the export possibilities of the less-developed countries and territories and of Japan, while at the same time avoiding disruptive conditions in import markets."[7] This gave rise to the LTA signed by nineteen countries and which was made effective from October, 1962, for a five-year period. The important feature of this arrangement was the specific incorporation of the concept and definition of 'market disruption' as discussed in the above paragraph.

The two main operating provisions of the LTA are:

a. *Article II:* That participating countries which still maintain import restrictions other than duties undertook to relax them and thereby expand the access to their markets. More importantly, the arrangement also provides the method by which to accomplish this elimination of import restrictions. It specified that not less than the following percentage increases over 1962 would be reached by 1967 by the following countries: Austria — 95 percent; Denmark — 15 percent; EEC — 88 percent; Sweden — 15 percent.

b. *Article III:* Authorizes participating importing countries which have not imposed restrictions to limit imports of specified cotton textile goods when these imports were found to be disrupting or threatening to disrupt their domestic textile markets. The importing countries are obliged to call for consultation with the exporting country (or countries) and in that consulta-

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[4] G. Verbit, *Trade Agreements for Developing Countries*, Columbia (1969), p. 59.
[5] *Ibid.*, p. 58.
[6] GATT, *Basic Instruments and Selected Documents*, Geneva (1961).
[7] GATT, *The Activities of GATT, 1961/62*, Geneva (1962), p. 29.

tion, request the exporting country to impose export restraints on the products causing disruption. Failing agreement on export restraints, the importing countries could impose import restraints, the level being determined by the provision made in Annex B of the Arrangement.

What underlies the basic acceptance of the LTA by the cotton textile exporting countries when it was first ratified in 1962? The generally agreed reason was their hope that it might result in "an appreciable increase in their access to European markets."[8] The European countries, especially members of the EEC, have consistently resorted to high tariff barriers against cotton textile exports from Japan and other low-wage exporters. Another reason was that the exporting countries "feared that unless something was worked out in an international forum, the United States and others might unilaterally impose even more stringent import quotas on their exports. They also hoped that by insisting on provisions for periodic reviews under GATT auspices they could introduce a liberalizing influence."[9]

A third and more important reason must lie in the exporting countries' hope that the importing countries would undertake the structural adjustments which would make the LTA unnecessary. That is, the LTA was viewed as a makeshift measure by which the importing countries like the United States, the United Kingdom, Canada, and the EEC countries could smooth the so-called disruption of their domestic markets so as to enable them to undertake the necessary steps to transfer resources out of their non-competitive cotton textile industries into other lines of production where they enjoy a comparative advantage.

The United Kingdom, the United States, Canada, and West Germany have concluded bilateral agreements with various cotton textile exporting countries since the LTA came into force.

What are the effects of the LTA and the various bilateral quota agreements ensuing from it on the exports of cotton textiles from the developing countries and Japan?

Firstly, it could be said that the LTA in fact provided a virtual charter of restrictions against the exports of manufactured cotton textile articles from the developing countries and Japan. This is derived from the way the term 'market disruption' has been defined in the Arrangement. What amount constitutes a sharp increase in imports of cotton textiles and at which price are the imported cotton textiles considered to be substantially below those prevailing for similar goods in the domestic markets of the importing countries? Also, what is the criterion of 'serious damage' suffered by the domestic producers when imports of cotton textiles increase?

An official in the Trade Division of the Ministry of Finance in Singapore illustrated this difficulty of interpretation when one of the Scandinavian countries 'warned' Singapore against further increases in textile exports to that country because imports into that country of textiles from Singapore recorded a rise by 200 percent over the preceding year, but in absolute terms, the increase was a matter of only S$2 million or so.

Secondly, and related to the first criticism, the Arrangement implicitly accorded a unilateral right to the importing country to determine when market disruption occurs or worse still, when the threat of a market disruption arises.

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[8] G. Patterson, *op. cit.*m p. 310.
[9] *Ibid.*

Thirdly, as correctly pointed out by Patterson, the import quotas existing in the EEC countries at the time the LTA was ratified were so low that even the commitment to double them by 1967 was considered by the exporting countries "as bordering on fraud."[10]

Fourthly, as Verbit points out, the LTA has eroded "a cardinal principle of international trade theory, that low labour costs are not a legitimate ground for restricting imports. They could not be if the theory of comparative advantage is to have any real meaning, for an excess of labour and the resulting low labour costs are a factor of production, which are crucial in determining comparative advantage."[11]

Finally, as could be implied from the renewal of the LTA for a further three-year period up to 1970 and subsequently the renewal took on an annual basis, the concept of 'structural adjustments' may not necessarily be the one hoped for by the exporting countries. It could very well mean that the importing countries hope to gain sufficient time to enable their domestic cotton textile industries to get on their feet by increasing productivity through higher capital intensity. As Patterson sees it, "if this results in either such low costs as to make the current special restraints unnecessary even from the producers' point of view, or so increases productive capacity as to strengthen the demands for continued protection, perhaps at levels somewhat below those now prevailing, the less-developed countries will conclude that the textile arrangement has been a cruel hoax."[12]

The recent U.K. announcement in July, 1969, bears testimony to the reservation made by G. Patterson that the LTA may prove to be a 'cruel hoax.' The quotas on cotton textile exports by Commonwealth countries to the United Kingdom will be replaced by a new tariff system: 6.5 percent on yarn, 15 percent on fabrics, and 17 percent on most garments, thus placing cotton textiles on par with the tariffs on synthetic textiles. These new tariffs will in fact extinguish the present system of Commonwealth preferences in respect of cotton textiles. Mr. Anthony Crosland (the then President of the British Board of Trade) was quoted to have said: "The tariffs will provide a margin of protection that is both stable and predictable, so enabling the industry to plan ahead with confidence."[13] This could be read as an attempt to buy time for the Lancashire industry to rationalize itself and to overcome some of its major problems — obsolete equipment, low productivity, and fragmented organization.

The unfavourable aspect of their new tariff system so far as Commonwealth countries like Hong Kong, Singapore, Malaysia, India, and Pakistan are concerned, is that these tariffs will not be applied to Britain's partners in the EFTA. This will give a decisive advantage to countries like Portugal over the Asian textile producers. The remarks of a textile producer in Hong Kong serve to illustrate the intense feelings of Asian textile producers: "We are all too well aware of how Portugal, a country which has no ties with the United Kingdom beyond those provided by EFTA membership and which has labour costs lower than ours, has gained an extra-favourable position in the U.K. textile market, largely at our expense. The ten-year period of sacrifice on our part in accepting quantitative restrictions on our textile exports to the United Kingdom has benefited not the U.K. textile industry,

10 G. Patterson, *op. cit.*, p. 311.
11 G. Verbit, *op. cit.*, p. 61.
12 G. Patterson, *op. cit.*, p. 317.
13 "Textile Exporters in a Spin," in *Asian Industry*, September 1969, Far East Trade Press Limited, p. 39.

but Portugal, which will be able, under EFTA agreements, to continue to export to the United Kingdom duty free."[14]

How has the LTA affected the textile industry in Singapore? So far, Singapore has entered into bilateral agreements on restraints, on cotton textile exports with the United States, the United Kingdom, and Canada.

United States

The first agreement was made effective from 1 April, 1966, until 31 March, 1969. Under this, "for the first limitation year, constituting the twelve-month period beginning April 1, 1966, the aggregate limit shall be 30,000,000 square yards."[15] Of this aggregate, 20 million square yards were to be filled by the increasing apparel category and 10 million square yards by the non-wearing apparel category (the specific breakdown is given by Clause (4) of the Schedule).

Clause (7) provides for a 5 percent increase in the subsequent twelve-month periods.

However, the first Agreement was superseded by a second Agreement which was made effective from 1 January, 1968, until 31 December, 1970. This new agreement provided for the first limitation year an aggregate limit of 36 million square yards (24 million in wearing apparel category and 12 million non-wearing apparel category). An annual 5 percent growth of quota levels was also provided for.

The third and latest Agreement was signed on January 19, 1971, and is to be effective from 1 January, 1971 until 31 December, 1974. For the first limitation year, the aggregate limit is 44,850,000 square yards (of which 29,900,000 square yards are for the wearing apparel category and 14,950,000 square yards for the non-wearing apparel category).

As the number of items in the wearing apparel and the non-wearing apparel categories have progressively increased with each new agreement, it means that more and more specific items have come under quota restrictions.

An analysis of the share of the U.S. total quota level enjoyed by the different countries could be fruitful in the sense that it could provide us with the rationale with which the U.S. government allocates quota levels — whether the levels are tied to past performance of each recipient country or whether non-economic considerations did play a part for certain countries like South Korea and Taiwan. But this has not been attempted because of two limitations: (a) data and information are not complete; (b) the first and subsequent Agreements between the United States and the various exporting countries were signed at different time periods.

However, an attempt is made to measure the performances to quota granted ratio in the case of Singapore — to provide an insight into the restrictive effects of the quota restrictions in terms of the fulfillment of these quota levels.

Apart from the first period, the exports of cotton textiles (quota items only) to the United States have consistently been below the actual quotas granted. Such under-utilization of quota levels could be attributed to:[16]

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[14] *Ibid.*

[15] First Quota Agreement: *The Singapore Cotton Textile Industry Restraint Schedule*, Clause (2).

[16] H. S. Narulla, "Singapore's Textile Trade and Industry (Manufacturing)" An Academic Exercise Submitted to Dept. of Econ., U. of Singapore, October 1969, p. 39-40.

i. The absence of domestic production of certain items in the quota agreements — for example, items 42 (other T-shirts), 48 (raincoats of 3/4 length or over), 49 (other coats), and items 18/19 (rain cloth shirting carded).

ii. The low production in certain other specific items (like items 45, 46, and 52) which is caused by: (a) the lack of adequate modern machinery to produce, for example, permanent press apparels; (b) the classification of such items being too general, such that differences in sizes and shapes, cuttings, etc., result in rejection of the product or overshipment of some products and undershipment in others. A specific example is that of 'work shirts,' which have almost similar cuttings as 'sports shirts' except that the latter have a tail end whilst the former have a covered tail end; (c) shifts in tastes for certain items — this results in a decline in these exports, whilst the quota items remain unchanged: a case at hand is that of the shift in tastes from cotton to permanent press pants; (d) the general lack of marketing strategies and the reluctance of local producers to establish or employ marketing agencies in the United States. This led to inadequate orders being obtained.

As regards the total U.S. textile quota granted to Singapore, it is perhaps fair to say that the over-all level seems substantial relative to Singapore's young textile industry. However, there seems to be a need to change some of the specific items under quota restrictions.

United Kingdom

Britain imposed import quota restrictions on cotton textiles in 1966, and the scheme was divided into two sections:

i. Country quota: which is allocated to individual countries;

ii. Global quota: which is world-wide and British importers are given restricted licences for obtaining cotton textile goods from any country but a specific limit is assigned to the amount obtainable from any one country.

This quota scheme was intended to last until 1970 and will be replaced by a 15 percent tariff duty on imports in 1972.

Singapore was granted a quota level of 3.8 million square yards (3.3 million square yards country quota plus 0.5 million square yards special country quota) with an annual growth rate of 1 percent.

From the above table, it could be seen that again, like the case of exports to the United States, there is underutilization of the quota levels granted, except that the degree of underutilization is much higher, especially in 1966, 1967, and 1970. Very much the same reasons could be put forth to explain such underutilization of quota levels here as with the United States. An additional factor may be found in the U.K. government announcement in 1969 that "import deposits have to be made for textiles. The new rule requires that half of the cost of the goods to be deposited with the British customs before they could be collected. The deposits will be returned only after 180 days."[17]

[17] Reported in *Singapore Trade and Industry*, Straits Times Press, January 1969 p. 31.

Canada

Quota restrictions on 100 percent cotton and polyester (and cotton-polyesters, whatever the degree of blending) garments — shirts and trousers — were initiated on 16 July, 1968 on Singapore's exports to Canada. The first Agreement or Memorandum of Understanding was made effective for the three twelve-month periods ending on December 31, 1968, 1969, and 1970. This has subsequently been renewed to cover the twelve-month period ending 31 December, 1971.

The quota levels granted are specific with no growth swing provisions like the United Kingdom and U.S. quota agreements with Singapore. The first Agreement specified a restraint annual level of 22,000 dozen shirts and 60,000 dozen trousers (including slacks, shorts, and jeans), whilst the new agreement specified corresponding levels of 28,000 dozen shirts and 62,500 dozen trousers. This second Agreement also included an extra item under quota restraint — that of cotton towels and towelling other than terry towelling with a restraint level of 64,000 pounds.

Performance in terms of fulfillment of the Canadian textile quota levels is better than that for the United States and United Kingdom, for the first two years at least, where a more than 90 percent fulfillment was recorded in 1968 and 1969. However, the 1970 exports fell short of the quota level by nearly 9,000 dozens. This could have resulted from the fact that local producers in Singapore "still face marketing problems since the shift in tastes to more advanced fabrics, which the local producers are as yet unable to produce."[18]

The major criticism of the Canadian quota system is that it only provides a 5 percent growth swing for Japan and Hong Kong, whilst the rest of the countries with which Canada has bilateral agreements do not enjoy such a provision. Not only does it contravene the terms of the LTA (where Annex B provides for a 5 percent annual growth swing),[19] but it also will eventually lead to a distortion of the market shares enjoyed by the exporting countries. Japan and Hong Kong will undoubtedly carve out a larger share of the Canadian textile market over time vis-à-vis the rest of the exporting countires, like Singapore or India.

3.1 Liberalization of Cotton Textile Imports by Developed Countries

The restrictive effects of the LTA have been discussed in Section 2. It seems rather obvious that one important way by which cotton textile trade could be liberalized is the accelerated relaxation of import quotas placed on cotton textiles from the so-called low-wage producing countries like Japan, Hong Kong, South Korea, India, Pakistan, Malaysia, and Singapore. One of the basic objectives of the LTA is to bring about an expansion of the less-developed countries' export trade in cotton textiles. The 5 percent growth swing provision in the LTA has not been observed by some of the importing countries in the bilateral agreements with the exporting countries. Moreover, no time limit has been imposed on the life of the LTA. It was originally

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[18] H. S. Narulla, *op. cit.*, p. 48.

[19] In this respect, the U.K. agreements also contravene the terms of the LTA as they provide for a 1 percent growth swing.

intended to be a five-year agreement to prevent cotton textile market disruption, but it has been renewed subsequently, at first for a further three-year period until 1970, after which the LTA became renewable on an annual basis. What was originally intended to be ephemeral appears to have become a permanent feature of the textile trade.

The latest turns of events have not been very encouraging for trade in textiles as a whole. Firstly, there was the imposition of a 10 percent surcharge on all imports into the United States by the Nixon administration. Although the surcharge does not affect those cotton textile items already under quota restraint, it may have restrictive effects on cotton textile items which do come under quota restraints. Secondly, the United States has unilaterally asked for restraints on exports of man-made textiles and apparels by Japan, Hong Kong, and South Korea. Japan acceded to the U.S. demand by announcing voluntary export restraints of these items at the beginning of this year. Hong Kong followed suit but her restraint level was not acceptable to the United States.[20] This second development could very well lead to a long-term arrangement to regulate the trade in synthetic textiles.

Although much emphasis has been given to the inhibitive effects of the LTA on cotton textile trade, there are also other commercial policies used by the developed countries to obstruct free trade in cotton textiles, the most important of which is the use of tariff barriers. Many excellent theoretical analyses have been made by Harry Johnson, Bela Balassa, G. Basevi, W. M. Corden, and others to show that not only are nominal tariff rates imposed on imports of importance, but that in terms of protective power, effective tariff rates are much more important. Effective rates are related to value added by manufacture after taking into account duties paid on material inputs. Table 11 shows the nominal and effective rates of protection for cotton textiles imposed by the United States, EEC countries, and Japan.

Therefore, another frequently discussed means by which the trade flow in the cotton textiles from the developing countries to the industrialized countries could be increased is a reduction in tariffs on the manufactured cotton textiles products like woven cotton fabrics and cotton clothing. It is to be noted that during the Kennedy-Round on tariff reductions, "because of the import sensitivity of textiles in general here (the United States) and abroad, the cuts made by the U.S. and other importing countries averaged less than 25 percent . . . and many textile products were excluded altogether."[21]

3.2 Liberalization of Trade Among Developing Countries

As seen, the actual turn of events in the developed countries' commercial policies may not be encouraging for trade liberalization — the LTA has been extended on an annual basis for an indefinite period, the United Kingdom will possibly enter the European Common Market, and the United States has undertaken some rather drastic steps to solve her balance of payments difficulties.

"It is clear that the development of an export trade in manufactures from developing countries depends primarily upon the efforts of these countries themselves."[22]

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[20] Reported in the *Straits Times*, 16 and 17 September, 1971.
[21] H. Lary, *Imports of Manufactures from Less Developed Countries*, NBER (1968), p. 125, footnote 14.
[22] UNCTAD, *Towards a New Trade Policy for Development*, U.N. (1964), p. 75.

One way in which the low-wage countries could expand the markets for their cotton textile manufactures is to reduce their protective tariffs not only on such products, but also on all the other manufactured goods produced by the developing countries as a whole. As UNCTAD rightly states, "In order to improve substantially the allocation of resources among developing countries, measures for the reduction of trade barriers should have the broadest possible scope, if trade were conducted in water-tight compartments, there would be a tendency to divert resources into inefficient channels."[23] In other words, liberalization of cotton textile trade can more easily come about if there is a multilateral reduction in tariffs on all manufactured goods produced by the developing countries themselves as a measure of self-help.

Table 12 shows the level of nominal tariffs imposed by some of the developing countries against the imports of cotton textiles. Although the coverage of countries in the surveys undertaken by the International Trade Centre is not complete, nor is the range of cotton textile exhaustive, the Table does indicate a common practice among the developing countries to impose high tariff barriers against cotton textile imports, mainly for import-substitution and employment-creation reasons.

High tariff barriers are also put up against the import of other manufactured goods[24] by the developing countries. Presumably a multilateral reduction of tariff rates among developing countries on the whole range of manufactured goods would enable individual country specialization in certain manufactured products according to comparative advantage vis-à-vis the other developing countries. The scaling down of protective tariff barriers against manufactured products may need to be made applicable only for imports from developing countries (and thereby maintaining a discriminatory tariff structure against the imports of manufactured goods from the developed industrial countries), especially in the transitional period. This is tantamount to the 'infant industry' argument for tariffs, but applicable to the developing countries only.

In more concrete terms, as is often suggested, multilateral tariff reductions could take place on a regional basis; for example, through the formation of an Asian or South-East Asian Common Market or Free Trade Area akin to the European Common Market or EFTA. However, political, sociological, and other non-economic differences may prove insurmountable for such a sweeping economic change. Bilateral agreements between developing nations should not be ruled out in respect of textiles and other commodities.

Another method of trade liberalization among developing countries which may prove less problematic is a unilateral adjustment of investment criteria by individual textile producing countries. For instance, Japan has moved away from the production of less-sophisticated textile items like low- and medium-grade garments, thus releasing a substantial market for exporters from other textile-producing countries to TAP.[25] Singapore has now dropped the textile industry as a priority industry, presumably because of the tight labour market, and the granting of licences for investment in textiles has

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[23] UNCTAD, *Trade Expansion and Economic Expansion Among Developing Countries*, U.N. (1966), p. 5.

[24] See International Trade Centre country surveys, *Market for Manufactured Products from Developing Countries*, GATT-UNCTAD.

[25] "Dark Clouds over Textiles," *Asian Industry*, May 1969, p. 41-5, Far East Trade Press Limited.

become more selective. To maximize the backward and forward linkage effects of investment in textiles, licences are now granted for fully integrated mills and for the production of texturized synthetics.[26] This policy is in line with the government's objective of encouraging the growth of more capital-intensive industries.

If the developing countries make serious attempts to align their investment policies according to the principle of comparative advantage, instead of putting up tariff walls for almost all lines of manufactures, the trade in cotton textiles and in all other types of manufactured products among the developing countries could expand and, in the long run, such a policy would be advantageous to trade and development to the developing as well as the developed nations in a more closely knit world economy. However, what seems obvious may seem idealistic in the face of the stark realities of the world, but that does not mean that men should not "still pursuing, still achieving, learn to labour and to wait."

TABLE 1

Singapore Total Trade[1] and Textile Trade[2], 1964-70
($ million)

Year	Total Trade			Textile Trade		
	M	X	Total	M	X	Total
1964	3,478.7	2,771.9	6,250.6	338.0	195.1	533.1
1965	3,807.2	3,004.1	6,811.3	330.4	190.9	521.3
1966	4,065.7	3,373.6	7,439.3	363.3	179.6	542.9
1967	4,406.5	3,490.6	7,897.1	483.3	173.1	656.4
1968	5,083.8	3,890.7	8,974.5	685.0	204.6	889.6
1969	6,243.6	4,740.7	10,994.4	799.1	259.0	1,058.1
1970	7,533.8	4,755.8	12,289.6	881.0	259.1	1,140.1

Source: *Singapore's External Trade Statistics*, Department of Statistics, various annual issues.

Note: [1] Excluding trade with Indonesia.
[2] Textile here refers to only Group 65 (textile manufactures or fabrics of all sorts) and Group 84 (clothing or wearing apparel) of the Standard International Trade Classification.

[26] According to Mr. Wan Ming Seng, Projects Analyst, Economic Development Board, Ministry of Finance, Singapore.

TABLE 1a

Singapore: Value of Textile Exports as a Percentage of Value of Total Exports, 1964-70

Year	Value (percent)
1964	7.0
1965	6.4
1966	5.3
1967	5.0
1968	5.3
1969	5.5
1970	5.4

Source: Derived from Table 1.

TABLE 1b

Singapore: Annual Change in Value of Textile Imports and Textile Exports (percentage terms), 1964-70

Year	Textile Imports	Textile Exports
1964-65	-2.2%	-2.1%
1965-66	9.9	-5.9
1966-67	33.	-3.6
1967-68	41.	18.1
1968-69	16.	26.5
1969-70	10.2	0.03

Source: Derived from Table 1.

TABLE 2

Singapore's Textile Trade, 1964-70: A Breakdown into Local Production, Local Consumption, Retained Imports, and Re-Exports ($ million)

Year	Textile Imports (M_T)	Textile Exports (X_T)	Textile Trade	DC_t[1]	DP_t[2]	CDP_t[3]	R-M_t[4]	R-E_t[5]
1964	338.0	195.1	533.1	172.9	30.0	7.3	165.6	172.4
1965	330.4	190.9	521.3	177.6	38.1	10.6	167.0	163.4
1966	363.3	179.6	542.9	230.8	47.1	16.8	214.0	149.3
1967	483.3	173.1	656.4	370.5	60.3	25.3	345.2	138.1
1968	685.0	204.6	889.6	585.5	105.1	39.6	545.9	139.1
1969	799.1	259.0	1,058.1	684.9	144.8	58.7	626.2	172.9
1970	881.0	259.1	1,140.1	n.a.	n.a.	n.a.	n.a.	n.a.

Source: [a] *Singapore's External Trade Statistics*, various annual issues, Chief Statistician, Department of Statistics, Singapore.
[b] *Report on the Census of Industrial Production*, various years.

Note: [1] DC_t — Domestic Consumption of Textiles = $M_t - X_t$ plus DP_t.
[2] DP_t — Domestic Production of Textiles (including footwear, except rubber footwear).
[3] CDP_t — Domestic Consumption of Domestically Produced Textiles.
[4] R-M_t — Retained Imports of Textiles = $M_t - X_t$ plus $DP_t - CDP_t$.
[5] R-E_t — Re-exports of Textiles = $X_T - DP_t$ plus CDP_t.
n.a. — not available at time of writing.

TABLE 3

Singapore's Textile Trade by Main Groups with Selected Countries, 1964-70
(in S$.000)

1964

	IMPORTS			EXPORTS		
Countries	Textile	Clothing	Total	Textile	Clothing	Total
Austria	1,086.1	165.0	1,251.1	—	0.6	0.6
Belgium Lux.	544.7	2.3	547.0	—	—	—
Cambodia	—	—	—	1,443.6	38.7	1,482.3
China	32,407.0	16,642.4	49,049.4	—	—	—
Formosa	1,286.7	2,057.1	3,343.8	3.5	0.4	3.9
Germany Fed. Rep.	7,000.6	226.6	7,227.2	—	38.7	38.7
Hong Kong	34,586.5	20,603.0	55,189.5	26,711.8	4,838.0	31,549.8
Japan	102,329.8	9,127.1	111,456.9	168.7	55.1	223.8
Sabah	4.4	0.8	5.2	5,550.1	4,810.2	10,360.3
Pakistan	2,988.8	40.7	3,029.5	6.5	11.3	17.8
Sarawak	6.7	0.1	6.8	7,110.5	4,074.7	11,185.2
U.K.	10,787.1	1,508.1	12,295.2	14,822.7	9,373.7	24,196.4
U.S.S.R.	8,135.9	—	8,135.9	—	—	—
U.S.A.	4,680.0	4,211.3	8,891.3	814.4	248.2	1,062.6
West Malaysia	8,078.4	1,536.1	9,614.5	80,774.4	14,852.6	95,627.0
Total			270,043.3			175,748.4

(Cont'd on p. 202)

TABLE 3 *(cont')*

1970

Countries	IMPORTS			EXPORTS		
	Textile	Clothing	Total	Textile	Clothing	Total
Austria	5,872.3	579.5	6,451.8	—	39.0	39.0
Belgium Lux.	5,604.4	15.3	5,619.7	987.9	12.7	1,000.6
Cambodia	—	—	—	716.0	6.0	722.0
China	107,995.5	10,958.0	118,953.5	0.6	1.5	2.1
Formosa	40,534.6	2,181.2	42,715.8	1.3	—	1.3
Germany Fed. Rep.	18,894.7	535.2	19,429.9	3,623.5	1,139.3	4,762.8
Hong Kong	47,151.3	8,896.0	56,047.3	7,027.6	4,435.1	11,462.7
Japan	394,751.9	13,722.6	408,474.5	238.1	1,046.3	1,284.4
Sabah	—	—	—	7,887.7	7,591.7	15,479.4
Pakistan	46,785.6	633.5	47,419.1	275.3	72.7	348.0
Sarawak	2.1	—	2.1	10,979.4	5,953.0	16,932.4
U.K.	24,420.8	2,161.3	26,582.1	5,299.9	4,833.3	10,133.2
U.S.S.R.	27,431.6	—	27,431.6	0.5	1,061.0	1,061.5
U.S.A.	8,577.8	3,488.2	12,066.0	8,774.4	33,968.8	42,743.2
West Malaysia	17,245.2	11,505.7	18,750.9	87,474.1	7,835.0	95,309.1
Total			789,944.3			201,281.7

Source: Singapore External Trade Statistics (including trade with West Malaysia), compiled by Department of Statistics, Singapore, various annual issues.

Note: Textile refers to Group 65 of SITC: clothing refers to Group 84 of SITC.

TABLE 3a

Singapore: Textile Imports and Exports to the Selected Countries as a Percentage of Total Textile Imports and Exports, 1964-70

Year	Textile Imports (%)	Textile Exports (%)
1964	79.9	90.1
1965	86.6	88.0
1966	89.1	85.4
1967	90.2	82.4
1968	89.6	79.6
1969	90.9	79.7
1970	89.6	77.7

Source: Derived from Tables 1 and 3 and other statistics.

TABLE 4

Total Number of Establishments[1] in the Textile Industry of Singapore, 1964 – 1969

Textile Items	No. of Establishments					
	1964*	1965*	1966	1967	1968	1969
1. Manufacture of Textiles	65	83	6	11	21	27
2. Tailoring and Dressmaking			27	31	43	41
3. Manufacture of Clothing (excluding shirts)			28	27	45	53
4. Manufacture of shirts			20	22	40	34
5. Manufacture of other Undergarments			11	13	15	17
6. Other Manufacture of Made-up Textile Goods			5	6	9	10
Total Textile Establishments	65	83	99	110	173	182
Total no. of establishments in manufacturing and quarrying sector	965	1,036	1,159	1,236	1,626	1,753

Source: *Report of the Census of Industrial Production*, Chief Statistician, Department of Statistics, Singapore, Various years.

Note: [1] Only those Establishments employing 10 or more workers are included.

*Establishments manufacturing footwear, (except rubber footwear) are included in Total Textile Establishments in 1964 and 1965.

TABLE 5

Domestic Textile Exports of Singapore ($,000), 1964-69, to West Malaysia, East Malaysia and Overseas Countries

Textile Items	1964 W.M.	1964 E.M.	1964 O.	1964 T.	1967 W.M.	1967 E.M.	1967 O.	1967 T.	1968 W.M.	1968 E.M.	1968 O.	1968 T.	1969 W.M.	1969 E.M.	1969 O.	1969 T.
Manufacture of textiles	na	na	na	na	229	—	2,920	3,149	639	119	15,204	15,962	4,251	152	17,247	21,650
Tailoring and dressmaking (individual order)	933	471	7,214		18	8	63	89	24	—	69	93	18	—	95	113
Manufacture of clothing (other than shirts)	na	na	na	na	651	455	5,514	6,610	655	1,056	14,449	16,160	689	662	21,440	22,791
Mfg. of shirts	429	502	2,356		669	673	13,057	14,399	593	574	20,177	21,344	408	419	25,590	26,417
Manufacture of other undergarments	na	na	na	na	492	251	67	810	555	220	192	967	250	198	207	655
Other mfg. of made-up textile goods	na	na	na	na	49	1	438	488	57	2	665	724	68	4	1,686	1,758
Total value of domestic textile expt.	3,187	1,242	17,163	21,512	2,108	1,378	22,059	25,545	2,523	1,971	50,756	55,250	5,684	1,435	66,265	73,384
Total value of mfg. quarrying sector exports	108,048	29,347	656,703	794,098	129,220	47,597	735,340	912,674	109,972	52,527	851,027	1,013,526	122,990	72,080	1,776,139	1,971,209

Source: *Report on the Census of Industrial Production*, Chief Statistician, Department of Statistics, Singapore, various years.

TABLE 6

Number of Workers Employed in the Textile Industry[1] of Singapore 1964 – 1969
(as at June of each year)

	1964*	1965*	1966	1967	1968	1969
1. Manufacture of Textiles			666	1,027	2,832	3,674
2. Tailoring and Dressmaking			508	623	888	772
3. Manufacturing of Clothing (excluding shirts)	3,512	5,965	1,696	1,835	3,072	3,732
4. Manufacture of Shirts			2,346	2,499	2,972	2,893
5. Manufacture of other Undergarments			290	355	387	379
6. Other Manufacture of Made-up Textile Goods			107	298	392	595
Total Employment in Textile Industry	3,512	5,965	5,713	6,637	10,543	12,045
Total Employment in Manufacturing and Quarrying Sector	46,284	51,959	57,521	63,195	80,533	107,235

Source: *Report on the Census of Industrial Production*, Chief Statistician, Dept. of Statistics, Singapore, Various years.

Note: [1] Only those textile establishments employing 10 or more workers are included in the textile industry.

*Workers employed in firms manufacturing footwear (except rubber footwear) are included in figure on employment in Textile Industry in 1964 and 1965.

TABLE 7

Value Added in Textile Industry 1964 — 1969
($000)

	1964	1965	1966	1967	1968	1969
1. Manufacture of Textiles			1,985	3,434	6,710	13,613
2. Tailoring and Dressmaking			1,306	1,538	2,317	2,470
3. Manufacture of Clothing (excluding shirts)	10,311	11,732	2,192	3,269	5,419	8,789
4. Manufacture of Shirts			3,274	4,967	8,248	8,587
5. Manufacture of other Undergarments			658	801	793	811
6. Other Manufacture of Made-up Textile Goods			183	639	1,201	1,784
Total Value Added	10,311	11,732	9,598	14,648	25,271	36,054
Total Value Added in Manufacturing and Quarrying Sector	310,393	368,388	437,770	509,760	648,916	914,595

Source: *Report on the Census of Industrial Production*, Chief Statistician, Dept. of Statistics, Singapore, Various years.

Note: Value added in 1964-65 in the textile industry is inclusive of manufacture of footwear (excluding rubber footwear).

TABLE 8

Singapore's Exports of Cotton Textiles (Quota Items) to the United States 1966-70 (million square yards)

Period	Quota Level Granted	Exports of Quota Items
1/4/66—31/3/67	30,000,000	30,248,217
1/4/67—31/3/68	31,500,000	28,174,626
1/4/68—31/12/68	27,000,000*	24,674,747
1/1/69—31/12/69	37,500,000	35,920,100
1/1/70—31/12/70	39,375,000	34,774,986

Source: 1. Various Agreements with U.S. government.
2. Trade Division, Ministry of Finance, Singapore, unpublished data.

*Taken as 3/4 of first limitation year of Second Agreement (3/4 of 36,000,000).

TABLE 9

Singapore's Exports of Cotton Textiles (Quota Items) to the United Kingdom, 1966-70 (million square yards)

Year	Quota Granted	Exports of Quota Items
1966	3.8 million	1,126,000
1967	square yards	1,969,000
1968	with a 1 percent	3,551,424
1969	growth per	3,746,875
1970	annum.	1,889,855

Source: Trade Division, Ministry of Finance, Singapore, unpublished data.

TABLE 10

Singapore's Exports of Textiles (Quota Items) to Canada, 1968-70
(in dozens)

Period	Quota Levels*	Exports of Quota Items
16 July—31 Dec. 1968	46,000	45,304
1 Jan.—31 Dec. 1969	46,000	45,993
1 Jan.—31 Dec. 1970	46,000	37,381

Source: Trade Division, Ministry of Finance, Singapore, unpublished data.

Note: Recalculated to account for the exports of Singapore before the middle of May, 1968. A total deduction of 12,000 dozen shirts and 96,000 dozen trousers was made. This worked out to an annual deduction of 4,000 dozen shirts and 32,000 dozen trousers for the three-year period.

TABLE 11[1]

Nominal Tariff Rates and Estimated Effective Rates
on Imports of Cotton Textiles (by Stage of Manufacture)
by the United States, EEC, and Japan
(%)

SITC No.	Product[2]	Nominal Tariff Rates			Estimated Effective Rates on Value Added		
		U.S.	EEC	Japan	U.S.	EEC	Japan
6513	Intermediate product — cotton yarn and thread	13.1	10.0	5.6	32.8	31.4	13.9
652	Finished manufactures — cotton fabrics, woven	17.5	15.0	10.5	31.2	27.5	20.0
841	Finished manufactures — cotton clothing	26.6	18.5	26.0	48.1	28.1	40.3

Source: H. Lary, *Imports of Manufactures from Less Developed Countries*, NBER (1968), p. 120-1.

Notes: 1. Rates relate to tariff structure prior to completion of Kennedy-Round of GATT negotiations.
2. Raw inputs for the cotton textile industry are usually imported free of duty.

TABLE 12

Nominal Tariff Rates on Imports of Cotton Fabrics and Undergarments by Certain Developing Countries

Country	Cotton Fabrics (%)	Women's and Children's Undergarments (%)
Thailand	40	40
Malaysia	25	25
Philippines	Grey 50 Bleached 75 Other 100	
Qatar	2.5	2.5
Ivory Coast*	71.1	71.1
Cameroon*	94	94
Liberia	20	34
Kuwait	4	4
Ghana	40	40
Saudi Arabia	20	25
Taiwan	cotton piece goods, grey 41.5 ditto, dyed 45 ditto, printed 45 ditto, yarn-dyed 45	knitted cotton underwear 55 other knitted cotton 70 cotton underwear, not knitted 70

Source: *Market for Manufactured Products from Developing Countries*, International Trade Centre, GATT-UNCTAD, Country surveys, 1969 (except Taiwan, 1970).

Notes: *These countries have lower tariff rates on imports of the above items from the Franc Area and the EEC.

COMMENTS BY PROFESSOR G. HAINSWORTH

Professor Hainsworth questioned whether the explanations, that were primarily concerned with the effects of the Long Term Agreement on Cotton Textiles (LTA) and that were offered for the disappointing performance of the textile industry, were in fact complete. He first took note of the development of the industry.

Historical precedent is not a good enough reason at this time for choosing the textile industry as a leading sector in a development programme. It was introduced into Singapore in the 1960s largely for its labour-absorptive capacity as indicated by Professor Lim's figures that it accounts for 11 per cent of employment but only 4 per cent of value-added. Unless it can increase its contributions to value-added, it is not pulling its weight in the economy. The reasons why textiles seem to be an obvious sector to start with are, first, related to the high income elasticities of textiles, particularly with high fashion turnovers. Since a high percentage of textiles are imported, it is seen as a good area for import substitution. Since there is a wide range of capital intensities in the industry, a less developed country hopes to enter the industry and move around in areas of the industry with different capital intensities, as Hong Kong has, and gradually move toward the high technology end of the industry. This explains why the industry is easy to enter, why it is difficult to move into other countries' markets, and since the high productivity end of the spectrum is very competitive, why it is difficult to move into this area.

Singapore went into the textile industry very late and faced competition from Hong Kong, Japan, Taiwan, India, Pakistan, China and Australia. The Asian Development Bank gave loans of questionable value to Singapore, especially since it should have been obvious that Singapore plants would be extensions of Hong Kong firms and would thus plow little in terms of profits or investments back into Singapore. Singapore's textile industry has a lot of idle, excess plant; it works only one shift; and highly monopolized control by Hong Kong parents has led the lethargy and a lack of aggressive production, selling and management techniques, especially since it plays second string to Hong Kong.

Professor Lim's three complaints about the constraints under which the Singapore textile industry must operate seem selective conjecture. Evidence that the LTA holds up exports seems unsubstantiated by Singapore's failure to fulfill quotas by large margins, especially as the European Economic Community has allowed quotas to double. *Ex ante*, Singapore and others should not have expected the developed countries to use the LTA to phase out their textile industries rather than to rationalize them to secure the high productivity end of the spectrum for domestic industry. Moreover, if Singapore-produced textiles cannot retain a hold on their own domestic markets with buoyant demand, it is unlikely that they will be able to make large inroads in the developed countries' markets. Singapore is a massive importer from all its textile rivals — from China, Japan, Pakistan and Taiwan — while those of Hong Kong grew only slowly because of interlocking ownership. Singapore's exports to Hong Kong and Taiwan fell to one-third the 1964 level by 1970 and although exports to Japan and Pakistan grew, it maintained a heavy trade deficit. Furthermore, Singapore did better by the LTA than others like Hong

Kong. Therefore, in this case it is not adequate to blame external constraints for poor performance. It is necessary to prove that external constraints operate no matter what the level of performance and that they increase with a better performance, which in the Singapore case cannot be proven.

The less developed countries need imaginative entrepreneurship and aggressive selling if they are going to get sustained growth and, for that, they need an on-going process of technological change while avoiding dead-end industries where chances of moving around the labour-capital isoquants are restricted and where more established rivals have economies of scale and research and development. These countries, especially those with a highly educated labour force, for some leading sectors must find a part of the technological frontier and become the world centre for specific products. This will lead to technological spillovers and an expectation of technological change and will avoid the second-best mentality that goes along with taking worn-out industries from more developed economies. Otherwise industrial development is a lost cause.

COMMENTS BY DR. HELEN HUGHES

Dr. Hughes said these two papers illustrate a number of important issues in trade from the point of view of the less developed countries and how these issues relate to the reactions of the developed countries.

The less developed countries are not a homogeneous commodity. They range from those just entering the development process and exporting activities, such as Hong Kong twenty years ago, to the level of Hong Kong today. Singapore shows that not all developing countries have to go through the whole process of development. They may enter manufacturing and exporting at different stages or levels of technological and managerial ability and capital accumulation. Many enter exporting when they have already built up an export structure. Hong Kong has been free trade from the beginning, whereas Singapore was one of the most protectionist countries in the early 1960s when it was concerned with the development of the Malaysian market. When it separated from Malaysia in 1965, it overnight became an ardent free-trader, but at that time, its earlier protectionist policies had not yet distorted the economy so the shift was made fairly easily. However, this shift will be much more difficult for many less developed countries in Latin America and Asia which have had import-replacement policies for a long time and now want to shift out into world trade.

The textile industry illustrates the problems of how these countries get into international trade. Hong Kong has moved into high grade textile products from the garment industries requiring high labour-intensity and low levels of organization and skills. One of the interesting ways Hong Kong has got around restrictions and quotas on its products has been by investing in textile production in other countries, notably Singapore, thus keeping up its profits. There are important economies of scale in the garments industries, so Hong Kong keeps the best orders and longest runs while giving the odds and ends of runs to its subsidiaries in Singapore. This explains why, in spite of the increased categorization of quotas, Hong Kong can fill its quotas and Singapore cannot. Moreover, since Hong Kong's corporate tax rate is 15 percent while Singapore's is 47 percent the parent firms shift profits from Singapore to Hong Kong. Thus Hong Kong has introduced new textile industries into a number of Asian and other countries and now Singapore is doing likewise.

Hong Kong and Singapore have a comparative advantage over the developed countries in many products. They have similar or more advanced technology, good management and commercial services, experienced labour and low wage levels. In items in which value-added is significant, they can jump over any tariff barriers, that look at all reasonable, that the developed countries can put up and this is why the developed countries have moved from tariff barriers to quantitative restrictions. Both Hong Kong and Singapore also have a comparative advantage over other less developed countries which are just beginning and do not have the know-how. Having to compete with these countries as well as the developed countries makes life difficult for the least developed countries although they are moving into the lower productivity, labour-intensive goods like textiles, furniture and electronic assemblying and forcing Hong Kong and Singapore into more capital-intensive industries.

This movement of less developed countries into high technology areas, despite tariff barriers, is what is really going to hurt the developed countries in coming years. This will likely lead to a proliferation of voluntary restraint agreements.

The danger with stressing the creation of too much labour-intensive industry is oversupply of these goods — banana republics become pyjama republics, although for countries like Indonesia there may be no alternative. But the lesson of Hong Kong and Singapore is to use the income, both private and social, from these labour-intensive exports to diversify into higher productivity capital intensive products. This, of course, has implications for expenditures on education, incentives to manufacturing and so on. The World Bank has made projections of a 15 per cent per annum growth rate in exports of manufactures by the less developed countries because this represents roughly the demand ceiling for this type of goods. The actual potential growth rate is closer to 20 or 25 per cent. The Hong Kong and Singapore experiences indicate that while the overall impact of the less developed countries exports on the developed countries' markets is small — about 3 per cent in the EEC and 5 per cent in the U.S. for textiles in general —, for specific products it is often high — for example, cotton knit shirts take up 20 per cent of these markets. However, at this point the developed countries will simply cut the market short and the less developed countries will have to get around this problem by changing their export structures. When nations like India or Brazil, capable of very large quantities of exports, get moving, Dr. Hughes foresees the saturation point of 5 per cent for general markets and 20 per cent for specific ones coming up very quickly and there will be a strong effect by developed countries to stop imports at that level.

If the less developed countries as a whole are going to be able to trade with the developed countries on an effective scale, there must be a new stress on adjustment assistance in developed countries to allow such changes in trade to take place. The marginal productivity of workers in Hong Kong and Singapore is higher today than the marginal productivity of workers in the U.S.A., Australia and many European countries. It is easier to retain the Singapore and Hong Kong workers who are, on the whole, better educated than the workers who will be displaced in the garment industry in the Southern U.S. Consequently, adjustment assistance needs to be a much broader policy than the training of a few thousand workers here or there, so that in fifteen years time, when this question becomes acute, there will be a new basis for world trade rather than the economic confrontation that could lead to very serious political consequences.

COMMENTS BY PROFESSOR D. SHERK

Professor Sherk said the subject of industrial development has been looked too much from the upper end of the product cycle and these two studies looking from the bottom end of the product cycle are very welcome.

It was said in the first session that adjustment assistance will be the most important question facing the developed countries in the 1970s. Professor Sherk was very pessimistic that the U.S.A. and other developed countries would be able to cope with adjustment assistance adequately. The experience of adjustment assistance in the U.S. under the Trade Expansion Act has been dismal. From 1962 to 1969, the U.S. Tariff Commission received twenty-six applications for adjustment assistance and all were turned down. From 1969 to 1971 only nine firms have been assisted and about the same number of labour groups. In all, no more than ten thousand workers have been helped by this programme.

From the U.S. experience in the 1960s there is evidence that the 1970s will be truly bleak in this area. During the 1960s the U.S. was undergoing expansion of employment in defence and space programmes and this expansion was directed to low capital intensive areas, such as Massachussetts and the Southern U.S. that were having trouble with textile and shoe production and permitted these areas to shift into higher technology industries. But, there are no such large government programmes on the horizon for the 1970s. Moreover, there is considerable pressure in the U.S. for protecting labour by means of either "voluntary export restraints" or quotas. The AFL-CIO is pushing for very tough legislation to limit imports of products from less developed countries. Finally, the institutions that are needed to deal with the adjustment assistance problem on a large scale do not exist; GATT cannot deal with it.

In discussing these problems, it is important to keep a notion of the product cycle in mind. For example, the multinational corporation can short-circuit the product cycle or, even more importantly, can provide the political clout to help the less developed countries by pressing the developed countries to keep their markets open, since the multinational corporations are operating in the less developed countries. This seems to be related to the textile industry which is very non-oligopolistic and in which the most problems are arising. In oligopolistic industries, the effects of protection can to some extent be offset through the political influence the multinational corporations have in Congress and in the political processes of other developed countries.

DISCUSSION

The trade policies of the less developed countries toward each other were said to be the result of a post-war reaction to the prewar division of labour. This reaction led to import substitution policies and very high tariffs among the less developed countries which make it difficult for these countries to trade with each other and are difficult to remove. The less developed countries have maintained mutual tariffs on textiles and all other products, but unfortunately much of the advice of development experts has been to develop common markets to exploit complementarity. Their mistake has been that it is when resources are competitive, not complementary that common markets are needed. A common market with complementary resources only increases the size of uneconomic units, such as in the Central American Common Market. The more difficult question of reducing tariffs has not been tackled because, while reduction of tariffs in rich countries with good social security at a period of high growth is not a serious problem, it is very serious in countries with huge employment problems, lower standards of living and so on.

In his reply, Professor Lim noted that ECAFE is now beginning to look for commodities that can tie nations together in a competitive rather than a complementary way. He thanked Professor Hainsworth for putting some doubt in his mind about the general restrictive effects of the Long Term Agreement and Dr. Hughes for her valuable insights. He said that the Long Term Agreement is a good instrument to faster short-term adjustment, although this applies to many policies, but that his fear was that the Long Term Agreement would become part of the long-term international trade scene and this would be most inappropriate.

A Japanese participant observed that it is difficult to distinguish 'Voluntary Export Restraints' (VERs) from export cartels in a comment on Professor Hsia's paper. The U.S. exempts export cartels from anti-trust legislation under certain conditions and many export cartels exist around the world. For example, he said in Japan there are roughly two hundred of which 30 percent were established to avoid foreign import restrictions, 30 percent to avoid excessive competition among exporters and 30 percent for both reasons. He said export cartels are as important a factor in restraining trade as VERs or quotas. He also agreed with Professor Hsia that the detailed classification of exports in VER agreements combined with the low swing allowances make it very difficult for exporters to respond quickly to changes in demand. This is an especially important problem in textiles where rapid changes in demand are common and was one of the main reasons for the breakdown of the U.S. — Japan textile agreement.

Professor Hsia replied to one comment on his paper that he did not say that without VERs, the diversification of industry and technological advances would not have taken place in the Hong Kong textile industry, but rather that it might have taken longer than without the pressure generated by VERs. He also gave an example of monopolistic practices interfering with the development of international trade. The development of spinning and weaving in Hong Kong was delayed for five years because of the cartelization

of synthetic fibre under a cartel agreement between ICI, Dupont and others which forced Hong Kong to accept monopoly prices from the designated supply source.

One participant from Australia emphasized Professor Sherk's point that the multinational corporations might be more sensible than many countries in the location of processing. However, another participant suggested that the multinational corporations have a role to play, but they do not always play the game according to competitive rules. The practice of giving tax concessions and creating tax havens causes such distortions in markets that one begins to wonder what the multinational corporations are actually trying to maximize and also to wonder who is benefitting from what. In their current term legislation to AFL-CIO have shifted their attack from textiles to the multinational corporations to end their double taxation privileges. When the trade unions hear that a multinational corporation is preparing to shift its production units to a less developed country, they threaten to strike all its plants in the U.S. This reinforced another participant's view below that adjustment assistance cannot be a part of a piecemeal approach to solving these problems but rather attempts to rethink the rules of the capitalist game are needed.

The problem of adjustment assistance to declining industries in the developed countries was a major topic of discussion. Another U.S. participant said that he was not quite as pessimistic as Professor Sherk about the future of adjustment assistance in the U.S., however, he agreed that the proposals of the AFL-CIO were indeed frightening. He also agreed that the U.S. Tariff Commission has tended to administer the adjustment assistance programmes badly, but emphasized that economists must do something very rapidly, using public relations methods, to promote acceptance of adjustment assistance programmes in the U.S. Also he suggested there is a greater tendency to use quotas against the imports of the less developed countries because the problem in the developed country is an employment and production problem which is affected mainly by quantities of imports but it is not a balance of payments problem which is more affected by value of imports. Moreover the less developed countries may prefer quotas to tariffs since they can raise their prices to just below developed country prices. Another U.S. participant suggested that better criteria were needed for adjustment assistance.

One U.S. participant suggested on one hand that there is a strong ideological bias in the U.S. against adjustment assistance. It is viewed as government interference with the free play of market forces while tariffs and quotas are not and are desirable. Business is reluctant to support legislation for adjustment assistance on these grounds while officials are reluctant because of the high budgetary cost although they have not done any cost benefit analyses nor considered the opportunity costs. On the other hand, he said Japan does have an effective industrial policy that shifts resources out of inefficient areas and pushes them into industries that have high future productivity. The U.S. claims it does not have an industrial policy, but in reality it does have such a policy made up of a number of *ad hoc* measures which end up protesting inefficient industry. The U.S. has rejected the Japanese approach as being government interference and direction of industry, but the Japanese approach is by far the more sensible.

A Canadian participant commented that, in federal countries, very strong provincial or state authorities compound the political reaction to this problem. Adjustment assistance in Canada is usually a matter of regional

development involving heavy capital and labour subsidies, but he said these subsidies may be just a new form of protection. While they are (one-time) subsidies, they are so large that they may have to be continued and they are often given to the very industries which the developing countries will want to develop in the next decade. His concern that what is intended to be an adjustment assistance programme will be soon turned into a new protection programme by businessmen was illustrated by Australia's 'devaluation compensation' programme which was rapidly built into something more permanent that intended.

Finally, another Canadian participant emphasized that the concept of adjustment assistance is not an easy set of policies that a government could adopt readily and it will not necessarily meet the problems, such as a better labour force in Hong Kong than in the Southern U.S. Solving problems such as this requires changes in the U.S. economy, in its education system, manpower training programmes and so on. It is not just trade that is a problem but rather that a more efficient capitalism is needed. This is again illustrated by the ideological problem mentioned above. Both the U.S. government policy of free education through to university and its policy of major support to research and development are indirectly aspects of U.S. industrial policy. They are not thought of as industrial policy, but they have far-ranging effects in turning out manpower and supplying large amounts of technology that contribute to the U.S.' comparative advantage in high technology industry. This type of broad government interference may have to be multiplied throughout all areas that affect industrial life.

Trade in Manufactured Products (II)

JAPAN'S NON–TARIFF BARRIERS TO TRADE IN MANUFACTURED PRODUCTS*

by

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1. Introduction: What are Non-Tariff Barriers?

Although the significance of Non-Tariff Barriers (NTB) to trade has been attracting increasing attention since the successful conclusion of the Kennedy Round, the concept of NTB has rarely been defined precisely. Very often descriptions of major types of NTB, rather than a definition of the term itself, are given to indicate what is meant by NTB. In view of the confusion in this area, I shall begin by stating my view on what is meant by NTB.

The phase NTB was coined by those who wish to promote free, multilateral international trade by reducing NTB, and thereby increase the real income of participating countries and to enhance mutual understanding and friendship. Thus interest in NTB originates from a pragmatic or policy point of view: the possibility of enhancing gains from international trade. Therefore, as a first approximation, NTB may be defined as "measures other than tariffs intervening in international trade, which distort the resource allocation of countries participating in world trade and thereby reduce their real income".

Authority to Negotiate

Although various customs, institutions or human organizations affect the pattern and volume of international trade, NTB covers only those regulatory measures which are taken by: (1) a central government; (2) local governments; and (3) non-governmental organizations such as trade associations, export or import cartels, or labor unions. Thus, the Japanese language or Japanese customs are sometimes held by foreign businessmen to be the most serious barriers to trade with Japan. They are not NTB. They are simply given data from an economic point of view.

Restrictive activities of business organizations are primarily the subject of anti-trust policies and are thus not considered to be NTB. However, when a non-governmental organization is empowered by the government or undertakes with the tacit consent of the government to impose restrictive measures on traders, such measures may be considered to be NTB. An example in Japan is the Japan Laver (seeweeds) Wholesalers Association's levying of

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*A paper presented at the Fourth Pacific Trade and Development Conference, held in Ottawa in October 1971.

Members of a research project on Japan's NTB sponsored by the Japan Economic Research Center made available to the author information underlying this paper and made useful comments on an earlier manuscript. The author is very much indebted to them.

import charges on imported laver from Korea to protect domestic laver producers and traders. The problem arose in the bilateral monopoly laver trade between Korea and Japan several years ago. Restrictive activities of export or import cartels often pose difficult problems.

For NTB to be established by local governments is unknown in Japan where the power of the central government vis-à-vis local governments is nearly omnipotent. NTB established by local governments sometimes present special difficulties in federal countries. For example, some U.S. states prohibit tangerine imports from Japan because of regulations imposing quarantines on imports of plants. Whether the prohibition is warranted or not, it is difficult for a foreign country to negotiate with each local government responsible for NTB.

Another problem concerning negotiations arises in situations where the Legislature and the Administration may favour different policies, and particularly when the Legislature tends to take international commitments lightly. Again this is no problem in Japan, where so far the Cabinet has been in a strong position vis-à-vis the Diet.

Legal Status

Whether a certain regulatory measure constitutes an NTB or not should be judged from an economic, rather than a legal point of view. We economists seek opportunities to increase economic welfare and gains from trade by reducing NTB. Whether NTB are legal international or not is a problem for lawyers not for economists. For example, most of Japan's import quotas on agricultural products are Residual Import Restrictions (RIR) which are in conflict with GATT, whereas U.S. import restrictions on agricultural products, which are also quite extensive, are not, as the U.S. obtained a waiver on these restrictions. But when the problem is to identify an NTB and to assess its welfare costs from an economic point of view, its legal status is a different matter.

Direct and Indirect NTB

Some NTB interfere with imports and some with exports. Let us first consider NTB on imports. Here we shall distinguish between "direct" and "indirect" NTB. In the case of a "direct" NTB, the regulating authorities (mostly the central government) take measures which discriminate against international transactions (imports) in favour of domestic transactions (domestic products) in order to promote domestic production and to suppress imports substantially. Tariffs and tariff quotas in themselves are not included in NTB by definition, but customs procedures or assessment systems containing special trade-barriers in addition to the tariff rates, are to be considered NTB.

Typical examples of "direct" NTB are: import quotas, the import deposit system, state trading enterprises, buy-national policies, discriminatory export or import financing, and so on.

An "indirect" NTB is a measure which is supposedly necessary to attain a certain desirable policy objective, and does not directly discriminate between domestic products and imports, but contains a substantial (sometimes prohibitive) trade-barrier element as a secondary effect. In intergovernmental discussions of NTB, very often the following situation arises: foreign countries charge that a country's use of indirect NTB is detrimental to inter-

national trade, while the government of the country in question argues that its instrument is not an NTB, because its purpose is not to reduce imports but to achieve a certain other desirable objective.

The problem here is whether the other objective is really desirable, and whether it cannot be achieved by alternative measures which do not seriously affect international trade.

For example, the purpose of quarantine regulations on animals and plants is not to reduce international trade, but to protect the country from diseases and insects. Sometimes imports of certain agricultural products from infected areas is totally prohibited. Very often, no alternative is available, besides the effort of exporting countries to exterminate the diseases or to invent treatments which prevent contagion. It must be pointed out, however, that the use of quarantine is sometimes abused.

NTB on Exports

In any country, we observe a striking asymmetry between policies regarding exports and imports. Almost every government tries to promote exports and restrict imports. Why this asymmetry obtains is an interesting socio-political question. The asymmetry is reflected in the GATT, which is much stricter on export subsidies and dumping than on import tariffs, and is lenient on export taxes or export cartels. From a national welfare point of view, for example, dumping by foreign countries in the domestic market may well be welcome, unless its purpose is predatory (which is impossible in most cases). But here as in many other situations the government and the public confuse the interest of particular industries or firms with the national interest. On the other hand, dumping abroad and subsidizing exports are generally detrimental to national economic welfare, although there are several exceptions.

We are concerned with NTB, because we think by reducing them world real income can be increased through improvement in the pattern of world trade and resource allocation. We should be concerned, therefore, not only with those measures which reduce international trade below an optimal level, but also with those which artificially increase trade beyond it. For this reason, non-tariff "distortions" may be a better word than "barriers" or "obstacles".

Quantitative restrictions on exports and minimum price systems for exports, introduced either by the government or by trade associations, are typical NTB aimed at reducing export. Examples of distortions which artificially promote trade are: subsidies of various forms on exports or on domestic production of exports, favorable tax treatment of incomes from export, and governmental financing of exports (and imports).

The primary purpose of most NTB measures is not to block trade but to achieve some other economically or socially desirable objective. Even in the case of the most direct NTB measures, such as import quotas, the purpose may be, to help small producers who are suffering hardship or to establish a promising infant industry. The problem here is how to separate necessary, unavoidable or justifiable measures from those that are not.

Free market mechanisms do not always lead to optimal resource allocation. Welfare economists enumerate cases of market failure to promote welfare. NTB are relevant to this problem. Non-economic policy objectives and intervention to achieve them cannot be dismissed by economic arguments.

Therefore whether a measure resulting in restrictive effects on trade is an NTB to be abolished or at least modified, depends on how one answers the following three questions: (1) whether the measure contributes to better world resource allocation in the long run: (2) whether the policy objective of the measure is "reasonable": and if the answer to the previous question is yes, (3) whether better alternatives are available. If investigation of these three questions leads to a conclusion that there is some possibility for improvement, the measure in question constitutes an NTB to be removed or modified. If there is no immediate alternative it should not be considered as an NTB.

A judgement concerning the above questions depends on one's general outlook on economic policy, so that it is very often difficult even for disinterested economists to reach agreement on what are NTB and what are not.

2. Import Quota and Trade Liberalization

Quantitative restrictions on imports, or import quotas, are a most explicit form of direct NTB and it was perhaps the most important NTB restricting Japan's manufacturing trade until recently.

Quantitative restrictions on imports may be classified in two categories according to whether they are legally admitted under the GATT or not. Those which are in conflict with the GATT are called Residual Import Restrictions (RIR), and the Japanese government's Trade (Import) Liberalization Policy in recent years is aimed primarily at reducing the number of items under RIR.

Japan's efforts at import liberalization began somewhat later than those of European countries. The government announced the "General Program" for liberalization in 1960, and adopted the "negative-list" system in 1962 in place of a "positive-list" system. The latter enumerated import items free of quantitative restrictions, whereas the former lists those for which quota restrictions are enforced.

Table 1 gives the liberalization rate for 1958-70, the ratio of liberalized imports to the total value of imports. Table 2 gives a summary picture of the liberalization process since 1962, before which comparable data are not available. From Tables 1 and 2, it will be seen that the liberalization policy has been eagerly pursued between 1960 and 1963, during which the liberalization rate jumped from 44% to 92%. From 1964 to 1969, only a few items were liberalized and the number of BTN 4-digit items under Residual Import Restrictions remained around 120. This was a period during which the Japanese government's efforts at liberalization were nearly suspended. As the basic trend in Japan's balance of payments changed towards continued surpluses after 1968, and foreign countries put more and more pressure on Japan to liberalize import restrictions, the government renewed and accelerated its liberalization effort with the cabinet's decision to continue import liberalization in December 1968.

Several factors influenced this policy change: the balance of payment surplus, the rapid and continuing rise in consumers' prices amounting to 6 to 7% per year, and pressure especially from the U.S. as well as other foreign countries. But the most important factor in this decision was the growing protectionist tendency in the U.S. Before the Japanese-American textile negotiations, and several anti-dumping cases from 1969 to 1970 in the U.S., in which imports from Japan were attached, neither the Japanese Govern-

ment nor the general public seriously recognized the fact that the very existence of the Japanese economy depends upon free, multinational world trade.

Although government officials and leading businessmen paid lip service to free international trade, there prevailed in Japan a belief that free world trade mainly benefits the most advanced, most "powerful" countries such as England in the 19th century, or the U.S. today, and is not necessarily beneficial to much less advanced countries such as Germany in 19th century, or Japan (and other less advanced countries) today. A corollary to this theory was for Japan to sabotage its obligations as a member of GATT or OECD to liberalize trade until foreign pressure became too strong and necessitated Japan's policy change. Now that the U.S. is beginning to turn towards protectionism many Japanese for the first time realize that Japan benefits a great deal from free world trade, and that it is to Japan's own advantage to establish and maintain free, harmonious, multilateral trade relations. In my opinion this realization is the most important factor behind the renewed liberalization effort in recent years.

The Present State of RIR

In 1968 when the number of RIR was 125 in terms of BTN 4-digit items, agricultural products (BTN Chapters 1 to 24) accounted for 69, minerals (25-28) for 8, and manufactures (29 to 99) for 48. By the end of 1971 at the latest, the number of RIR will have been reduced to at most 40, of which 9 items are manufactures. The process of import liberalization of manufactures since 1969 is given in Table 3. The reasons why RIR on each item listed in Table 3 was maintained until recently are various, but are generally the same as the reasons for high tariff rates in any country: the weak competitive power of a declining domestic industry, an infant industry situation (real or imaginary), the existence of strong foreign firms dominating the world market, and so forth. But, although I do not have the detailed information on individual items, my general impression is that the reasons for protection seem unwarranted in most cases and that the effort towards liberalization began too late.

When the number of RIR on manufactures is reduced to 9 at the end of this year, 4 will be related to leather, another 4 to electronic computers, and the remaining one is integrated circuits (IC).

The leather industry embraces very small producers from a special, low-income, socially discriminated group, and in view of their low mobility to other sectors, the government judges that liberalization of these four items is socially undesirable for the time being.

The Japanese domestic market for electronic computors is about equally divided by foreign and domestic producers (counting Japan IBM as foreign). The four leading Japanese computor makers have a market-share of about 10% each, but they are still substantially behind IBM especially in larger scale computors. At present, under strong pressure from the U.S., the Japanese government is considering further liberalization in this field perhaps for terminal and accessory units, and smaller computors.

I am no expert on the computor industry, but I am sceptical of the merit of early liberalization in this field. Here IBM occupies a dominant, near-monopoly position in the world market. I fear that too early liberalization may simply lead to IBM's dominance and monopoly of the market. In an industry where technological progress is rapid and the economies of scale

are important, and where few very large firms dominate the world market, a country's protective policy to bring up viable competitors may lead to improvement in world resource allocation rather than the other way round.

Liberalization of a certain item is sometimes accompanied by a raise in the tariff rate on that item or the introduction of a tariff quota system, provided that the item is not covered by the GATT rate so far. This has occurred, however, mainly for agricultural products, minerals and primary metals, rather than for manufactures. Secondly, such substitution of tariff barriers for NTB took place mostly before 1964. The fact that one cannot simply raise tariffs as a substitute for NTB is another achievement of the Kennedy-Round.

Import Restrictions Other than RIR

There are 48 items (BTN 4-digit) on which quantitative import restrictions other than RIR are imposed by the Japanese government. Namely, 11 items under GATT Article 17 (the state trading enterprise), 10 items under Article 20 (b) (protection of human, animal and plant life, and health), 3 items under Article 20 (c) (gold and silver), and 27 items under Article (b) (national security) are under direct import restrictions.[1] Some of these "lawful" non-liberalized items are essentially the same as RIR from an economic point of view. Especially government trading in rice, wheat, butter, milk and other dairy products achieves the same result as RIR. Therefore, if one is concerned only with conformity with the GATT provisions, simply turn RIR into state trading, and the problem will be "solved".

Among manufactures covered by these lawful quantitative restrictions, the following items appear to have a substantial NTB element: vaccine, blood serum, airplanes, aeronautic radio equipment, gunpowder, and hunting guns. To consider light airplanes, gliders, any airplane engines and radar equipment as "military weapons" endangering national security is obviously far fetched. The Japanese government is now considering liberalizing light airplanes, radar and aeronautic radio equipment.

The Relative Importance of Quantitative Restrictions

It is difficult to assess to what extent these RIR and other quantitative restrictions hinder Japan's import trade. Although the number of RIR has been declining, quantitative restrictions still cover a substantial part of imports, as seen from Table 4. For every half-year period, the government announces the total size of the import quota and its breakdown into four categories: foods, mineral fuel, machinery and others. The last two columns of Table 4 give the ratio of import quotas to the value of actual imports for the overall import total and for machinery. It shows that the liberalization rate given in Table 1, which is computed with fixed 1959 weights means very little for recent years. This is because the composition of imports has changed very much since 1959. RIR have covered certain income-elastic imports such as meat, prepared foods, coking coal, refined petroleum, machine tools and computors. Also, apparently, the government has been increasing the size of quotas for these items under the quota system as a move towards freer

[1] Since one 4-digit item includes several items which are under restrictions for different reasons, the summing the numbers of items for individual reasons do not add up to 48. Also of these 48 items, 5 overlap RIR, so that the net addition to the total of non-liberalized items is 43.

trade. The ratio will decline in 1971, as a result of the extensive liberalization put into effect in 1970 and 1971.

3. Non-Tariffs Barriers on Imports Other than Quotas

In Japan, although there are numerous NTB other than import quotas, none of them, according to my impression, is comparable in its relative importance. In the following we shall briefly describe some of the more important ones.

Subsidies and Excise Taxes

Both subsidies on domestic production and excise taxes on domestic consumption reduce imports and unless there are justifiable reasons for them, they constitute NTB.

An example of such a subsidy in Japan, and perhaps about the only important example in the field of manufactures, is an interest subsidy on ocean-going ships owned by Japanese shipping companies and built by domestic shipbuilders under the government shipbuilding program. In my view, this is an unnecessary subsidy which cannot be justified for economic (and perhaps other) reasons. It constitutes an NTB. In this case, the barrier or obstacle is likely to be only nominal, since the Japanese shipbuilders build nearly one half of the world annual shipbuilding tonnage and are very strong exporters. To obviate the NTB, beginning from this year the government does not require companies to build ships in Japan in order to receive subsidization. But it is unlikely that Japanese shipping companies will build their subsidized ships abroad.

Examples of Japanese excise taxes which are called NTB by foreign countries (U.S., Canada, and U.K.) are the excise tax on larger passenger cars and the liquor tax on whisky. The scale of the *ad valorem* excise tax on passenger cars is based upon the cylinder capacity, and 15% is levied on cars below 2000 cubic centimeters, 30% on 2000-3000cc and 40% for those above 3000cc. The liquor tax on whisky cheaper than 700 yen per litre is a specific rate of 929,000 yen per kilolitre, while the rate for more expensive whisky is 150% for whisky worth 700 to 1000 yen, and 220% for whisky over 1000 yen per litre.

In both cases the formal reason is to restrain consumption of luxuries, and the excise rates apply whether home produced or imported. But passenger cars and whisky brands on which these luxury rates apply are produced in Japan only on a very limited scale, and these high rates are mainly for imports.

It would be difficult to justify the difference between these luxury rates and the rates for less expensive categories. Moreover, the tariff rate on whisky is very high: about 35 to 40% when converted to the *ad valorem* rate. Therefore the luxury in this case is not due to high costs of production but to tariffs. The reason for this high liquor tax appears to me to be protection for domestic producers. The protective effects of the liquor tax are in addition to those of tariffs on liquor which are generally very high.

The NTB aspect of these high excise tax rates has been recently challenged and the reduction in the rate on larger passenger cars will materialize in the near future.

Import Procedures

Foreign businessmen often complain of complicated import or exchange procedures and cumbersome formalities in Japan. This may be generally true, perhaps as compared with most other advanced countries. But I would like to point out two aspects of Japanese red-tape.

First, complicated formalities which require many forms and documents are not confined to international trade or foreign exchange procedures.

Among the various procedures concerning imports, I shall take up two which appear to constitute NTB: the AIQ system and the system of standard methods of settlement.

(i) Automatic Import Quota (AIQ)

In Japan in order to import any goods one must obtain an "import approval" certificate. All goods are classified into three groups: Import Quota, AIQ, and Automatic Approval (AA) groups. For goods in the AA group, one can receive the approval at any authorized foreign exchange bank (most commercial banks), which simply confirms that the goods in question are in the AA category. This procedure is useful for statistical reasons: the government and public can learn of the trend in imports much earlier than in other countries.

To import goods under the Import Quota one must obtain a quota permit which are allotted from time to time.

The AIQ category is an intermediate one, and when an IQ item is liberalized, it is shifted to AIQ before going on to AA. For goods in AIQ, MITI (Ministry of International Trade and Industry) is responsible for issuing the import approval, but in practice this is issued automatically within 3 or 4 days after applying to MITI. The name AIQ is misleading since there is no quantitatively limited "quota"

The formal reason for AIQ is to observe closely the trend in imports after liberalization, and also to calm down opposition to liberalization. But at least in recent years there has been no case in which an item is returned from AIQ to IQ after liberalization, or the approval of AIQ import has been delayed. Therefore, the system has, in fact, almost no practical merits. In view of the pressure from foreign governments, which is based mostly upon misunderstanding, the Japanese government is now considering abolishing the AIQ category and shifting the liberalized item from IQ directly to AA.

(ii) The Standard Methods of Settlement

Under Japan's exchange control system, only certain standard methods (terms, means of payment, period, etc.) of settling export and import accounts are automatically approved, and when one wishes to use settlement methods other than those prescribed as standard methods, one must apply to MITI for an individual approval. The system tends to be stricter on imports than on exports: for example, payment must be made within 4 months for imports and within six months (one year until recently) for exports. A large part of import transactions, perhaps more than 95%, are settled by standard methods. Thus, in principle, the system is to the advantage of a domestic machine tool maker *vis-à-vis* a foreign one, for example, in extending medium-term credit to buyers. Advance payment is not within the standard method.

Japan's exchange control system is highly complicated and almost every businessman, not only foreign but also Japanese, is highly critical of its cumbersomeness. In the recent speculative attack on the yen, however, the rush on short-term capital was limited mainly to the "leads" effect on the export side and investment in bonds. Almost no "lags" effect took place on the import side because of the rigid, 4-month standard method of settlement.[2]

If a country sticks to the adjustable (or almost unadjustable) peg system, and wants to pursue an independent monetary policy and/or to avoid a heavy speculative attack on its currency, certain exchange controls to check short-term capital movement are in order. Restrictions on export and import settlement may be necessary for this purpose. A better solution would be to adopt a crawling peg with a wider band.

Government Procurement

There are no Buy National law such as the Buy American or Ship American laws in the U.S. There is a provision in a cabinet order stating that for a few stipulated articles the government may buy domestic products in preference to imports when the prices tendered are exactly the same. This provision, however, has never been applied in practice. In fact a wide range of imports such as printing machines, accounting machines, computors, typewriters are commonly used within the government (especially in the national universities, as professors like to have novel, foreign-made apparati).

Thus there is no formal discrimination in government procurement against imports or foreign suppliers, but in practice there is an inherent bias towards Japanese suppliers. This is because the government rarely invites an open, public tender, but receives tenders only from those nominated by the government. This is common not only with the central government but also with local governments and government enterprises such as the Japan National Railroad, Japan Telegram and Telephone Corporation, and the Japan Highway Corporation. Therefore, there are often complaints even among Japanese businessmen who feel that the government or government enterprises favor a particular firm or group of firms. Again, the problem here is not only the problem of fairness towards foreigners but also of fairness within Japan. But this is a difficult problem, since it is a custom in Japan to esteem and enjoy close and confidential personal relationships. It is difficult for ordinary Japanese to change suppliers from time to time simply because of prices.

The solution to the problem may lie in working out an international code on government procurement policies.

Administrative Guidance

"Administrative Guidance" (Gyōsei Shidō) is a vague word for discretionary advice, wishes, requests or sometime threatening orders by government officials given to private firms which are not based upon any clear-cut, well-defined stipulation in laws and ordinances. It must not be thought that in giving administrative guidance the government officials are doing something illegal. There is usually a vague, comprehensive stipulation in the law that a certain government agency is responsible for the orderly condition of a certain field and may take appropriate measures for maintain-

[2]For export settlement, the standard terms are less restrictive, and for example, advance payments are allowed.

ing it. For foreigners it might appear strange that Japanese firms accept such government officials meddling with private business affairs, but in a society in which the central government has traditionally such wide powers over citizens, it does not pay in the long run to be openly opposed to the government, or so most people think.

What kind of "administrative guidance" constitutes an NTB is difficult to ascertain, since such direction usually takes subtle forms and is not made public.

An example of the Japanese government's "administrative guidance" and perhaps the only clear-cut case pointed out by foreign governments, is concerned with large-capacity steam-power generators, turbines and boilers. Steam-power generating equipment of a size larger than a certain prescribed limit (200 thousand KW since 1962, and 400 thousand KW since 1964) were under quantitative restrictions until recently. When an electric power company built a power station and installed several units of generators, the government requested the power company, as a condition of the issue of an import license for the first unit, to ask the exporting American maker of that unit to make available a patent to some Japanese maker to produce the second and following units. This policy of "the first unit imported but the following units home-produced" has been severely criticized by the U.S. as a most obvious NTB. Now that the import of all steam-power equipment is liberalized, there is room no longer for such administrative guidance.

Such direct intervention into private business dealings is certainly contrary to the principle of free enterprise and is therefore generally undesirable. But from an economic point of view, there is an element of rationality in such a policy. Japan is technologically much less advanced than the U.S., and U.S. firms often have a monopoly position in the world in technologically strategic fields, based upon patents and know-how. To purchase advanced technology helps the propagation of new technology and increases the competitiveness of the market. The problem here is how to harmonize the conflict between technological propagation and increasing competition on the one hand, and a fair return and incentives to technological innovators on the other.

4. Non-Tariff Distortions on Manufactured Exports

On the export side there are three major kinds of non-tariff barriers or distortions to be described here briefly.

(1) Self Restraints on Export

Several laws exempt export cartels from anti-trust prosecution, and there are various types of cartels. Also, the Government does not approve the export of certain kinds of goods, unless certain conditions are met. These cartels and regulations are generally called "self-restraint on export" (Yushutsu Jishu Kisei). Apparently not all such cartels and regulations are NTB: for example, when exporting cameras, the exporter must show that he can offer a repair service to overseas users. Such restrictions may be justified to ensure certain standards for exports.

Typical reasons for cartels, however, are twofold: first, to avoid import restrictions from the importing country, such as an import quota, a raise in the tariff rate, a tariff quota or an anti-dumping measure: and, second, to lessen "excessive competition" among Japanese exporters and to establish

an "orderly condition" in the export trade. These two reasons overlap each other and are in practice difficult to separate. A cartel of this type regulates quantity and/or prices, and is often given either an exclusive right to export the goods in question to the export market under the cartelization, or is allowed to regulate outsiders (in the case of restrictions on price). Otherwise outsiders would nullify the very point of the cartel.

Much of such "self-restraint on exports" is called for either by the governments or industries of importing countries, and accepted unwillingly by Japanese exporters. They think self-restraint is better than higher tariffs or quantitative restrictions enforced by the government of the importing country. For cotton textiles which are under the Long Term Agreement, the export restriction is compulsory.

The self-restraint on export is an obvious NTB. It benefits foreign firms competing with Japanese exports and hurts consumers and the general economic welfare.[3] For example, the U.S. Government which is eager to pursue anti-trust policies for maintaining competition and is supposedly trying hard to stabilize the price level, has arranged a semi-official self-restraint on Japanese iron and steel exports, under which the annual rate of growth of Japan's iron and steel exports to the U.S. is limited to a mere 2.5%.

What percentage of Japanese export is covered by such restraints is not known to my knowledge, but my guess is that about one quarter to one third of all exports are under some quantitative and/or price restriction.

(2) Measures for Promoting Exports

There are several provisions in the tax laws the sole purpose of which is to encourage exports. A certain part of income from (0.5 to 2.3%, depending upon the size of the firm and upon whether it is a trading company or manufacturer) may be deducted from income and accumulated as a special reserve,[4] thereby reducing the taxable income of exporters. Also, exporters may apply a higher, accelerated rate of depreciation than ordinary firms. These two provisions are a remnant of the more extensive tax incentives given to exporters when Japan's balance of payments tended to turn into a deficit.

The government has two measures to promote exports through making low-interest credit available to exporters. First, a governmental financial institution, the Japan Export Import Bank, extends long and medium-term credit to exporters of machinery of all kinds including ships and tankers, at lower interests than available through commercial banks. Although the name of the Bank includes "Import", financing of imports amounts to only about 10% of the Bank's outstanding loans. The rest finance exports. Second, the Bank of Japan has rediscounted export bills at substantially favorable interest rates until very recently.

To achieve optimal resource allocation through the international division of labor, exports should neither be promoted nor discouraged, therefore these tax provisions and financial measures cannot be justified on purely economic grounds. In the beginning these measures were introduced for balance of payment reasons, and once introduced any such measure has

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[3] In some cases Japanese exporters who receive export quotas also gain because of higher prices.

[4] Entitled as the Overseas Market Development Reserve.

a strong tendency to persist, since vested interests are formed and oppose abolition.

Recently, Japan's balance of payments has turned into heavy surpluses. Most of these export-promoting measures have lost meaning entirely and have been losing public support. The government is now considering either abolishing or at least narrowing the range of these measures.

Discrimination against Japanese Exports

When Japan joined the GATT in 1955 a large number of countries, including most European members of GATT, invoked Article 35 against Japan: that is, they refused to enter into GATT relations with Japan. Many new states in Africa and Asia which were previously British or French colonies also invoked Article 35 against Japan when joining the GATT. At present, 22 countries, mostly in Africa, out of the 78 members of GATT, still invoke Article 35 against Japan, although some of them give Most Favored Nation (GATT) treatment to Japan.

A more serious case of discrimination against Japan at present is the so-called "negative-list" import restriction applied to imports from Japan by some European countries. Between 1963 and 1964 most European countries withdrew the application of Article 35 and entered into GATT relations with Japan.[5] But although most European countries now officially have GATT relations with Japan, many of them still maintain a negative-list against Japan (or against only a few countries, including Japan), in addition to non-discriminatory, global RIR. For items in the negative-list, these countries maintain quantitative restrictions on imports from Japan. The number of items on which each country maintains discriminatory import restrictions is difficult to ascertain, but according to a recent Japanese government source, it is as follows (in terms of BTN 4-digit items): Sweden 52, Italy 45, France 38, Norway 25, Benelux 22, West Germany 14, and Denmark 8.

Most of the items in the negative-list are manufactures such as various textiles (other than cotton, which is under the LTA), tires and tubes, belt conveyors, footwear, ceramic tiles, umbrellas, silverware, sewing machines, ball and roller bearings, radio and TV sets, porcelain insulators, automobiles (Italy), motorcycles, microscopes (France) and toys.

From Japan's point of view, these discriminatory measures which violate the GATT are the most difficult NTB to cope with. A third country pays little attention to the problem as its exports are not affected, while in the case of overall, non-discriminatory NTB several countries are directly involved and protest.

It must also be pointed out that the "self-restraint" on exports forced upon Japan by importing countries are very similar to the negative-list discrimination. Although generally self-restraint is slightly more flexible, and the premiums arising out of restrictions accrue to Japanese exporters somewhat more certainly under self-restraint, the overall effect of self-restraint and import restrictions against Japan by European countries are quite similar.

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[5] Austria, Ireland, Portugal, and Spain are still invoking Article 35 against Japan.

5. Concluding Remarks

The extent to which these NTB reduce below (or in the case of export promoting measures increase beyond) the optimum level the volume of import to and export from Japan and thereby hurt economic welfare is impossible to assess. Therefore the following remarks are based upon my general impression rather than a careful assessment of each item of NTB.

(1) It seems that after considerable efforts at liberalization by the Japanese government since 1969, Japan's NTB on manufactured imports are of minor importance. Although there still remains much room for further reducing NTB, their overall effect on Japan's imports are much less than the tariff-barriers to trade. This is certainly true for manufactures, but perhaps also true for non-manufactures if the staple foods (rice, wheat and barley) are not taken into account. It must be recalled that according to the recent tariff study by the GATT secretariat, Japan's average tariff level on manufactures was the second highest (next only to Australia's) among the eleven countries under examination. Also, the number of items (manufactures) to which a tariff rate higher than 10% or 12.6% was applied was the largest for Japan. Also Japan has quite a few tariff-quotas (mostly on agricultural products and minerals), which constitute fairly rigid trade-barriers.

(2) It seems that by now the trade-impeding effect of Japan's NTB on manufactured imports is much less than that of some other countries. In Japan there is no substantial NTB comparable to, for example, "Buy American" practices, the system of American selling prices, abuses of anti-dumping measures,[6] or variable surcharges on agricultural products as in Germany.

(3) Quantitative restrictions are the most important of Japan's NTB on the import side. But as far as manufactures are concerned, Residual Import Restrictions are by now limited to a few items. Electronic computors are one of the items under RIR, but it may not be advisable to abolish import quotas on computors immediately, in view of a monopolistic market structure in this field. Whether a policy measure constitutes an NTB should be judged from an economic point of view, not from its international legal status.

(4) Other countries' NTB measures against Japanese exports, including "self-restraint" forced upon Japan, seem to have much larger effects upon international trade than Japan's NTB, as far as manufactures are concerned. This may be so, even if non-manufactures are included with the exception of rice. If major trading countries agree to abolish all kinds of NTB on imports which are not justifiable on economic grounds, Japan's exports will likely increase more than her imports.

(5) Japan should make serious efforts to abolish or reduce any remaining NTB as well as tariff and tariff-quota barriers. Perhaps the reduction in tariff rates would have greater beneficial effects for Japan. Such an effort should be accompanied by policies to make the mobility of resources (especially labor) easier, and to compensate somehow for those unfavorably affected.

But to argue that such a policy of freer trade is desirable and that the government should adopt such a policy is similar to rats talking about

[6] The anti-dumping policy is another difficult subject concerning international trade policy, but my general view is that except against obvious predatory dumping and others having undesirable welfare effects, anti-dumping measures cannot be justified on economic grounds, and hence constitute NTB.

putting a bell on a cat. There are always vested interests associated with an NTB, and they oppose change in the status quo. Usually the adoption of individual NTB measures affects a small number of people favorably and a large number of consumers and the general public unfavorably. The favorable effects are densely concentrated upon the small group while the unfavorable effects upon the general public is thinly spread over a large number of people. Therefore, the political power which can be summoned by small interest groups seriously affected by any change in NTB or tariffs is usually greater than the counteracting power. The analysis of the political power of various groups in the process of economic policy making is, however, a subject of political science rather than economics. We economists are not well trained to deal with such a problem.

(6) There is no need, however, to be too pessimistic as far as Japan's NTB are concerned. Among Japanese policy makers and businessmen there has been a remarkable turn in thinking on this in the last one or two years. Although there still remain strong protectionist tendencies here and there, Japan's international trade policy will be moving towards lower trade barriers and freer trade, provided that world trade continues to expand and that other countries cooperate in the effort for freer trade, or at least do not move towards the opposite.

TABLE 1
Trade Liberalization Rate[a]: 1958-70

End of Fiscal Year			
1958	33%	1965	93%
1959	37	1966	93
1960	44	1967	93
1961	70	1968	93
1962	88	1969	94
1963	92	1970	94
1964	92		

Source: Ministry of Finance, *Monthly Statistical Bulletin*, various issues.

[a] Liberalization Rate is the ratio of the value (in 1959) of imports for which quantitative restrictions are removed. Imports under quantitative restrictions other than IRI are excluded both from the denominator and numerator.

TABLE 2
The Process of Import Liberalization: 1962-71

Date (month)		Major Items Liberalized[a] (manufactures only)	Completely Liberalized	Non-Liberalized[b] (RIR)
1962.	1		195	900
	4	Alloy steel*, petroleum coke, chemical pulp, fork-lift trucks, FM radios, electric welding machinery*	603	492
	10	Pulp for paper making, machine-tools* (middle size), toilet soap, fountain-pens	833	262
	11	Yarn of sheep's wool, knitted fabrics, crocheted fabrics, bed linens, synthetic fibres, carpets, power-shovels (mechanical-shovels)	841	254
1963.	4	Copper and articles thereof	866	229
	6	Accordions, felt hats	868	227
	8	Yarn of synthetic fibers, woven fabrics of flax, glass ware, pumps including motor pumps and turbo pumps, electric accumulators	903	192
1964.	1	Lauan wood and plywood, antibiotics*	906	189 (152)
	2	Unwrought zinc, unwrought lead, etc.	913	182 (145)
	4	Boilers, electric generators*, colour television receivers	921	174 (136)
	10	Bulldozers, tractors, colour photographic plates, etc.	933	162 (123)
1965.	10	Imitation precious stones, motor vehicles	934	161 (122)
1966.	4	Streptomycin, yarn of synthetic fibres	936	159 (120)
	5		928	168 (126)[c]
	10	Unwrought tantalum and articles thereof, penicillin, outboard motors* (within 20-25 horsepowers)	929	167 (124)
1968.	4	Tulle, lace, perfumed water, Eau de Cologne, toilet powder, perfumed cream, lipsticks, foundation water	931	165 (122)
	10	Alloy tool steel*, high speed steel*	932	164 (121)
1969.	4	Cast, rolled, drawn or blown glass, beet-pulp pellet, colour film for cinema, outboard motors	933	163 (120)
	10	Automatic printing machines, industrial sewing machines, Thermionic valves and tubes	935	161 (118)
1970.	2	Straw and products thereof, basketwork, woven fabrics of sheep's wool, automatic vehicles, chassis with motors	944	152 (109)
	4	Preparations of penicillin and streptomycin, fruits flavor, photographic film narrower than 35mm., boilers, machine tools, cranks, electric generators	955	141 (98)
	9	Ramie, synthetic precious or semi precious stones, Diesel engines, typewriters, digital type-electronic computers,* integrated circuits*	963	133 (90)
1971.	1	Color film for photographs, tool-tips and plates, sticks and the like for tool-tips, antibiotics (cycloserine, tetracycline etc.), embroidery (including motifs)	973	123 (80)
	6	Sodium glutamate, preparations with a basis of antibiotics; patent leather, articles of apparel of leather, wood charcoal, parts of footwear of leather, engines for motor vehicles	993	103 (60)

(Cont'd on p. 236)

TABLE 2 (cont'd)

9 (Planned)	Menthol, peppermint oil, dextrin, soluble or roasted starch, starch glues, prepared mordants, steam turbines (over 400 thousand KW), input units and output units designed to work in electrical connection with digital type electronic computers, telephone switchboards and exchange of electronic types, controller for system exchange	1.013	83	(40)

Source: Ministry of Finance, *Monthly Statistical Bulletin*, various issues.

[a] Asterisk (*) indicates partial liberalization.
[b] Includes partially liberalized items.
[c] Due to a technical change in the Tariff Table, as Japan joined the BTN Agreement.

TABLE 3
Reduction in RIR on Manufactures: 1969-71

	Date	BTN number	Items
1.	1969 Oct. (3 items)	84.35	Automatic printing machines
		84.41	Industrial sewing machines
		85.21*	Thermionic valves and tubes
2.	1970 Feb. (5 items)	46.02	Straw and products thereof
		46.03	Basketwork
		53.11	Woven fabrics of sheep's wool
		87.02	Second-hand motor vehicles
		87.04	Chassis with motors
3.	1970 Apr. (8 items)	29.43	Chemically pure sugars
		30.03*	Preparations of penicillin and of streptomycin
		33.04	Fruits flavor
		37.02*	Photographic film narrower than 35mm.
		84.01	Boilers
		84.45	Machine tools
		84.63	Crank shafts
		85.01	Electric generators (over 400 thousand KW)
4.	1970 Sept. (7 items)	54.02	Ramie
		71.03	Synthetic precious or semi-precious stones
		84.06*	Water-cooled Diesel engine
		84.51	Typewriters
		84.52*	Digital type electronic
		84.53*	computers under a certain size*
		85.21*	Integrated circuits
5.	1971 Jan. (4 items)	29.44	Antibiotics
		37.02	Color film for photograph
		58.10	Embroidery (including motifs)
		82.07	Tool-tips and plates, sticks and the like for tool-tips
6.	1971 June (7 items)	29.23	Sodium glutamate
		30.03	Preparations with a basis of antibiotics
		41.08	Patent leather etc.
		42.03	Articles of apparel of leather
		44.02	Wood charcoal
		64.05	Parts of footwear of leather
		84.06	Engines for motor vehicles
7.	1971 Sept. (8 items) (Planned)	29.05	Menthol
		33.01	Peppermint oil
		35.05	Dextrin, soluble or roasted
		35.05	Dextrin, soluble or roasted starch, starch glues, etc.
		38.12	Prepared mordants
		84.54	Input units, output units designed to work in electrical connection with digital-type electronic computers*
		85.13	Telephone switchboards and exchanges of electronic types
		85.22	Controllers for system exchange
8.	RIR at the End of September 1971 (9 items)	41.02	Bovine cattle leather and equine leather
		41.03	Sheep and lamb skin leather

(Cont'd on p. 238)

TABLE 3 (cont'd)

41.04	Goat and kid skin leather
64.02	Footwear with outer soles of leather
84.52*	Digital-type electronic
84.53*	computers
84.54*	The terminal machines for digital-type electronic computers
84.55	Parts of the digital-type electronic computers
85.21*	Integrated circuits

Source: Ministry of Finance, *Monthly Statistical Bulletin*, various issues.

*Partial liberalization of a BTN 4-digit item.

TABLE 4
Ratio of Import Quota to Total Import: 1964-71

Unit: million U.S. dollars

Fiscal year	Total Import (A)	Of which Machinery (B)	Import Quota Total (C)	Foods	Mineral Fuel	Machinery (D)	C/A (%)	D/B (%)
1964	6,327	464	1,413(100)	497(35)	293(21)	464(33)	22	7.3
1965	6,507	344	1,647(100)	692(42)	443(27)	344(21)	25	5.3
1966	7,738	424	2,049(100)	838(41)	597(29)	424(21)	26	5.5
1967	9,449	706	2,505(100)	800(32)	729(29)	706(28)	27	7.5
1968	10,447	806	2,667(100)	737(28)	814(31)	806(31)	27	7.7
1969	12,763	1,050	3,169(100)	757(24)	985(31)	1,050(33)	25	8.2
1970	15,407	1,836	4,475(100)	822(18)	1,430(32)	1,836(41)	29	11.9
First half of 1971	—	809	2,165(100)	361(17)	816(38)	809(37)	—	—

COMMENTS BY PROFESSOR H. E. ENGLISH

Professor English commented that Professor Komiya's paper concerns one of the key issues in the present controversy between the U.S. and Japan, yet Professor Komiya states that the facts of the matter are not nearly as strident as some people believe. A great deal more precision is needed in this area if the conflict this issue has generated is to be defused.

In neglecting to deal with the issue of export cartels and taxes, real problems of allocation of resources between primary and secondary industries are ignored. It is very doubtful if there is anything to be gained in the long-term allocation of resources by preserving the monopolistic practices of exports cartels. This issue never gets seriously discussed.

It is clear from page 8 of the paper that in Japan as in so many other countries what happens to the short-term balance of payments governs the pace of trade liberalization. When are these two areas going to be separated and when will the former be prevented from getting in the way of long-term efficiency?

Professor Komiya implies that the present U.S. government practices are the best means to get trade liberalization in Japan. Professor English wondered if Professor Komiya really agreed with this implication.

Professor English was very suspicious about whether, in an industry like computers, the traditional types of protection are going to be effective in enabling domestic industry to catch up to the U.S. especially if the industry is producing non-specialized types of computer and when it appears the Japanese market is already inefficiently divided up among four different companies.

Professor Komiya's comment about the maintenance of protection in primary metal industries by substituting tariff for non-tariff barriers raised questions in Professor English's mind about Japanese policy and attitudes. Professor English then asked if this reflected the view of the Japanese government and industry that it is always important to have vertical integration in mineral-based industries.

Professor English wondered if it was just a simple matter to turn Residual Import Restrictions into state trading to solve the problem of consistency with GATT.

Professor English asked for more specific comments on the relative importance of NTB's such as AIQ, the standard method of settlement, government procurement policies and administration guidance. He noted however that if Professor Komiya was correct and this whole category was not important, this request was also not important.

Finally, Professor English concluded that he was not yet convinced that these Japanese practices are as insignificant as Professor Komiya claimed, partly because of the number of complaints heard about these practices. He suggested that international companies need greater incentives and opportunities to operate in Japan so that they can afford to set up their own information-gathering facilities to gather the information required for doing business in Japan. He said that if Professor Komiya's conclusion, that tariff barriers really are still the most important obstacle to developing trade with Japan, is valid, then the U.S. tactics at present are even more inappropriate. He said that it is up to all concerned to give a better indication of the real importance of non-tariff barriers.

GOVERNMENT PURCHASING POLICIES, OTHER NTB'S, AND THE INTERNATIONAL MONETARY CRISIS

by

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The purpose of this paper is to make some broad recommendations concerning non-tariff barriers generally, and to examine in detail a specific non-tariff barrier: U.S. government purchasing policy toward foreigners. Given the dramatic events since August 15, 1971, one might consider such an essay to be of secondary importance, if not distinctly *mal à propos*. Our own view is, however, exactly the contrary. The present state of exchange-rate flexibility and the contemplated future state of exchange-rate realignment provide an ideal opportunity, if not an invitation, for all countries to eliminate non-tarrif barriers — to break the shackles of these myriad administrative impediments to the unrestricted movement of commodities and capital.

Part 1 below makes the case for the integral role which removal of non-tariff barriers should play in any package of reforms emerging from the present crisis. Part 2 describes U.S. government procurement policy as a particular example of a non-tariff barrier, and summarizes the results of the Appendix, in which the effects of this U.S. policy are measured both qualitatively in the framework of a theoretical model.

1. New Opportunity for Reducing Non-tariff Trade Distortions

One important potential benefit from the current floating exchange rate condition that has not been sufficiently stressed is the opportunity it provides for significantly reducing certain types of non-tariff distortions to international trade. To better understand the nature of this opportunity consider the three main reasons for the imposition of the non-tariff distortions that plague world trade. Sometimes all three reasons lie behind the introduction of a particular trade barrier, but usually one of the three is the major cause for a specific trade-distorting measure.

A first objective in introducing non-tariff trade-distorting measures is to provide aid to particular industries or sectors that either are under severe competitive pressures or are regarded as essential for a country's development or defense goals. Quantitative restrictions on selected imports and domestic aids to specific industries are common methods of implementing this objective. For example, the quotas on cotton textile imports into the U.S. and on coal imports into several European countries and Japan illustrate the use of non-tariff barriers as a means of furnishing assistance to relatively depressed sectors. The coal industry in Europe, Japan and Canada also receive direct subsidies from the government. Similarly, the use of quotas (allegedly) for defense reasons is illustrated by the quantitative restrictions on oil imports into the U.S., whereas aids for development purposes are exemplified by the subsidies to the electronics industry in France and Germany. In the developing world, of course, quantitative limitations on imports and subsidies on exports are the major instruments for promoting industrialization.

A second purpose for using non-tariff trade-distorting measures, which fortunately has not been too important in recent years, is to stimulate aggregate demand and domestic employment. A regrettable example of this rationale seems to be the recent proposal in the U.S. that the 10% investment tax credit be limited to investment goods produced in the United States. The initial objective of the "Buy America" act passed in 1933 was also designed primarily to stimulate domestic employment.

The third and final main objective of non-tariff trade-distorting measures is to improve a country's balance of payments. The recent imposition of a 10 percent surcharge on imports by the U.S. as well as the use of selective surcharges by Canada in 1962, a uniform import levy by the U.K. in 1967 and selective quotas by the French in 1968 illustrate this reason. Export subsidies, prior import deposit schemes, and outright exchange controls are also widely used in both developed and developing countries for balance-of-payments purposes. The tying of foreign aid, the strengthening of buy-national measures, and controls over foreign investment further illustrate this category. All three of these latter measures have, for example, been employed by the U.S. in recent years.

Clearly it is the third category of distorting policies (and to some extent even the first two) that should and can be promptly eliminated now that rates of exchange for some of the key currencies in the world are floating and, hopefully, moving toward equilibrium positions. The exchange rate mechanism can be relied upon to handle the balance-of-payments problem these measures were designed to help — and to do it in a manner that tends to raise world income. However, while this latter achievement, i.e., raising world income, is almost universally accepted as a desirable goal, in practice it is often difficult to implement because of resultant economic hardships to particular groups. But measures designed to improve a country's balance of payments usually do not focus on any particular group and thus can be eliminated without causing any significant redistribution of income. The impact of a uniform import surcharge or export subsidy tends, for example, to be so widely diffused that no industry or income group is greatly affected. This is a main reason why special uniform (or nearly uniform) import levies and export aids generally are politically relatively easy to remove after an exchange adjustment has been made. It is less obvious to the general public, however, that such measures as investment controls, preferential government purchasing policies, broadly based export subsidies and even such domestic aids as special investment grants or special depreciation allowances fall within the same category. A good case can be made that they should be eliminated, or perhaps in some cases, moderated, at the time of currency realignments. The income effects of these measures are also widely diffused and though their removal causes the loss of easy profits to some firms, these firms generally are able to adjust without suffering undue hardship. However, in those cases where there is a significant impact on particular firms and income groups, we must employ the other policy measure needed (in addition to greater exchange rate flexibility), if non-tariff trade barriers are to be significantly reduced, namely, an effective domestic adjustment assistance program.

Although non-tariff trade-distorting measures aimed at improving a country's balance of payments are the most obvious candidates for elimination, the reduction of non-tariff trade barriers should not stop there, especially in countries whose currencies depreciate. Measures directed at assisting particular industries and at stimulating aggregate employment can

also be eased, since the currency depreciation itself promotes these goals by stimulating exports and reducing imports generally. Indeed, it is imperative that such an easing of those NTBs directed at relatively depressed sectors be made. Otherwise the period of painful adjustment simply drags out longer. What may happen in the absence of a reduction in artificial import barriers is that employment actually expands temporarily because of the depreciation and a new generation of workers is made to endure the hardship and humiliation of spending a lifetime in a marginal industry.

In countries whose currencies tend to appreciate, the problem is somewhat different. Usually these countries have already eased their general surplus-generating trade barriers as well as those directed is stimulating aggregate demand. They may even have eased some of their trade distortions that benefit special sectors. However, when foreign goods become cheaper as their currencies appreciate, competitive forces operating on these sectors intensify so that political pressures tend to arise for an increase in the use of trade-distorting measures as a means of providing greater aid. This is a tendency that these countries and the world community generally must strongly resist. We must treat a period of currency realignment as an opportunity to meet legitimate adjustment needs by means that solve basic problems rather than merely postponing them. It means, in other words, that we must use the occasion to substitute realistic domestic adjustment programs for income-distorting international barriers to trade. Adjustment on dislocation assistance has been ignored too long, when in fact it is the least-cost means of aiding injured sectors of the economy.

The question is frequently asked: What "contribution" should the United States make in the process of realigning world currencies? Some argue that the U.S. should raise the price of gold. This, of course, provides a windfall gain in dollars to gold holders and tends to offset the capital loss on the dollar holdings of foreigners as the dollar depreciates. While such a change is perhaps not harmful to any country on either economic efficiency or absolute equity grounds, it is difficult to see how such a "contribution" is very helpful. Moreover, it tends to perpetuate a system whose drawbacks have just been dramatically illustrated.

A truly meaningful contribution on the part of the U.S. in terms of raising income levels both abroad and within the U.S. would be to remove promptly not only the import surcharges but the controls over foreign investment, foreign aid, and government purchasing policy that have been introduced in the last decade for balance of payments purposes. In this way the U.S. could emphatically reaffirm its commitment to a liberal trade policy, while still solving its international monetary problems by exchange rate realignment.. Moreover, the U.S. should not just stop with removing these controls. It should also seize the opportunity to seek international agreement for undertaking a vigorous effort to reduce other trade-distorting measures based on employment or protectionist grounds.

It is to be particularly hoped that the Japanese will also use this period of currency realignment to remove most of their remaining quantitative and administrative restrictions on imports. Many have appeared to be designed primarily for maintaining an undervalued yen rather than for protecting particular sectors that face severe difficulties in adjusting to greater import competition. Unless these controls are greatly eased at this time, the yen will tend to appreciate beyond its true equilibrium level and possibly cause long-run export problems for basically strong industries. Thus, by lifting these controls and making a contribution to the better use of world

resources, the Japanese can also moderate the appreciation pressures on the yen.

Of course, some difficult problems do arise for Japan, Canada, and others whose currencies are appreciating with respect to truly depressed industries in which real adjustment difficulties exist. Currency appreciation puts further competitive pressures on these sectors by making foreign goods cheaper and thus raises the demands for even more protection. As previously mentioned the answer to these demands should be greater domestic adjustment efforts rather than the greater use of adjustment means that pass part of the burden on to foreigners and merely perpetuate the underlying domestic problem. But we must be realistic and realize that the prospects for substantial progress in this area are much less favorable than in the area of trade barriers which have been raised primarily for balance of payments purposes.

2. Government Procurement Policy

That non-tariff restrictions for balance of payments reasons are extensive and significant, yet can be removed or greatly eased at this time, can be no better illustrated than with reference to government purchasing policies. When purchasing goods and services all governments seem to give preference — either formally or informally — to domestic producers compared to foreign suppliers. Moreover, when unfavorable balance-of-payments pressures build up, increasing the degree of these preferences is one of the first offsetting actions governments take.

The country against whom the most criticism has been voiced in the area of government purchasing policy is the U.S. Purchases by the federal government are covered by the so-called Buy American Act of 1933. This requires the procurement of domestic materials by U.S. government agencies unless: (a) the head of the agency determines this would be inconsistent with the public interest; (b) the agency head determines their cost would be unreasonable or (c) the materials are not available in the U.S. in satisfactory quantity or quality. In 1954 an executive order set forth implementing guidelines that defined materials to be of foreign origin if foreign products account for more than 50 percent of the cost of all products used in making the materials and that specified a domestic price as unreasonable if it exceeded the foreign price (including any tariff) by more than 6 percent (12 percent for small and depressed-area firms.)

Criticism of the U.S. increased sharply when in 1962 the Defense Department, because of the deteriorating balance-of-payments, raised the preference rate to 50 percent. The Defense Department also established a 50 percent preference rate for purchases of goods for use overseas, although the Buy American Act covered only items to be used domestically. AID and other federal agencies also adopted this figure. Beside these various federal restrictions on importing, a number of states and smaller governmental units have passed Buy American laws.

The laws of most other countries appear on the surface to be much more liberal than the U.S. Buy American Act. The U.K. permits preferential treatment of domestic producers under "special circumstances" but there is no general requirement for such treatment. Firms in depressed areas come under the "special circumstances" qualification. Certain nationalized industries also purchase abroad only if substantially better quality and lower prices are offered than from U.K. suppliers. French authorities contend that

foreigners are not treated differently than domestic producers except in a few limited cases. One is the electronics industry where the government has agreed to make a certain part of its purchases from domestic producers. Certain social groups, e.g., agricultural producer societies also are favored somewhat by the government. Such important trading nations as Germany, Japan and Australia also do not legally require government agencies to grant preferences to domestic suppliers except in a few limited circumstances, e.g. to medium-sized firms or firms in depressed areas.

When one examines purchasing practices and procedures more carefully, it becomes obvious that discrimination against foreigners is not simply a matter of buy-national laws that openly specify the preferential treatment of domestic firms. Consider the matter of bidding procedures. The U.S. favors the use of public tender. Under this procedure invitations to submit bids are advertised to the public at large and an unlimited number of suppliers can submit bids. Most other countries use selective bidding in which invitations are offered to only a limited number of potential suppliers on a list approved by the government. American producers argue that they find it difficult to get on the approved list and often fail to hear about a potentially profitable opportunity. Under public tender, on the other hand, the advertising of the forthcoming government purchases is likely to be more extensive and thus the chances for discrimination — either deliberate or inadvertent — are reduced.

The failure of such countries as the U.K., Germany and France to open bids in public so that the price and terms offered by the successful bidder are known to all is also listed by American firms as a factor that discourages their bidding for government contracts abroad. The companies claim they would gain more experience about how to prepare successful bids if this knowledge were available. Moreover, their fears of favoritism would be mitigated. However, these governments counter with the argument that collusion among suppliers would soon develop if all bids were disclosed. Still another obstacle that some governments introduce is a residency requirement on foreign suppliers.

In the actual analysis and evaluation of non-tariff barriers, a common complaint is that they are not susceptible to rigorous theoretical analysis. This is not true, however, in the case of discriminatory government purchasing policy, as we demonstrate at length in the appendix. To summarize just one of the conclusions presented there, consider the possible price and trade effects of a preference system, assuming that the commodity supplied by foreigners is identical to that produced domestically and that the government's demand is insensitive to price. Under these conditions, the price effect of granting preferences to domestic producers on government contracts can vary from none at all to a rise in price equal to the full amount of the preference. In the absence of a preference system, the domestic price of a particular product equals its export value from a foreign port plus insurance, freight, and duty charges on its entry into the domestic economy. A preference system imposed on top of tariffs diverts government purchases from foreign to domestic producers. As the preference causes the domestic price to rise above the foreign price, it also encourages diversion of private purchases from domestic to foreign producers. If in the absence of a preference system, domestic production exceeds government purchases of an item at its equilibrium price, the preferential treatment given to domestic producers will have no effect on the price of the product. Competition among producers will keep the price that the government pays

domestic producers the same as private purchasers pay. On the other hand, if domestic supply falls short of government demand, the competitive system will bring about a rise in the price that the government pays. However, should the supply of imports not be completely elastic, the price of imports to private consumers will fall.

The trade and domestic production effects also depend upon the relation between domestic supply at the pre-preference equilibrium price and the government's demand. If domestic supply is equal to or greater than government demand at the pre-preference price, no change in imports or domestic production takes place. If domestic supply is less than government demand as the pre-preference price, the output of domestic producers will rise, and imports will in this case fall.

A more realistic assumption than that import and domestic goods are identical is that they are imperfect substitutes. The appendix sets out an algebraic model capable of analysing this case, and the model is then applied to the problem of measuring just what have been the actual effects of government purchasing policy in the U.S. on imports — by no means a simple task. We will only summarize this analysis here.

On the basis of comparatively crude data available for a few countries, it seems clear that for comparable commodities the government's import ratio is much less than the private sector's. For example, in 1963 the total expenditure by the U.S. government on goods that move in international trade (excluding agricultural commodities, minerals, and armaments) was almost $25 billion. However, the direct imports of these goods by the government was only $61 million, or 1/4 of one percent of these expentitures. As has been shown elsewhere, these U.S. figures do not seem to be much out of line with those in other countries.

Using the model set out in the appendix, together with reasonably satisfactory estimates of the various parameters underlying it, we estimate that the "Buy American" program in government purchases reduced total U.S. imports in 1963 by between $76 million and $110 million, as compared to what total imports would have been in the absence of any government discrimination at all. Moreover, the potential for reducing U.S. imports by these means, by which we mean the maximum reduction in imports which could have been achieved by a total ban on U.S. government imports was only between $112 million and $164 million. Whether these import "savings" are substantial when compared to total U.S. imports in 1963 of just under $20 billion is questionable. At best, somewhat less than one percent of total imports could have been stemmed by discrimination against imports in government purchases, and the actual figure seems more like half of one percent. Whatever gain is attributed to the policy must then be offset against the costs in terms of higher tax burdens and reductions in the gains from trade.

3. Policy Proposals

As noted in the first section, the United States could make a major contribution in the world trading community by lifting the discriminatory margins against foreign purchases by the government that were established in the early sixties. However, in order to improve the purchasing practices of other governments as well as to prevent the tightening of the discrimination each time a country gets enmeshed in balance-of-payments problems, we must also adopt a code of fair practices on government purchases. The key principle is that government purchasing policies should — subject to certain

derogations — be based on non-discrimination against foreign products and suppliers of foreign products. In order to implement this general principle, governments must agree to a number of reforms in their purchasing procedures and practices. Public bidding should be employed to a much greater extent. Whenever selective tendering is used, vigorous efforts should be made to insure that all interested foreign suppliers have an opportunity to apply for inclusion on the list of potential bidders. Procurement notices should be more widely distributed, and time limits or technical requirements in these notices should not discriminate unnecessarily against foreign firms. Residence requirements for bidding should be liberalized. All bids under public and selective bidding procedures should be made public except where such action would clearly make subsequent collusion possible, would result in the disclosure of confidential information, or would result in significant administrative difficulties. Furthermore, rejected bidders should be given more information concerning the reasons why their bids were turned down than they presently are in many countries.

Discrimination against foreign producers for reasons of national security or public health should not be greater than necessary to implement those objectives. Discriminatory purchasing as a means of meeting balance-of-payments problems, of fostering economic development in depressed regions, and of assisting new or ailing firms should be discouraged.

There are also better ways of providing regional assistance or aid to new and depressed firms than by discriminatory government purchasing policies. Experience suggests, however, that the total volume of regional aid would decline, if this form were discontinued. Therefore, it seems appropriate to permit such assistance provided it is temporary and conforms with the rules established for government aids. Any preferences granted for these purposes or for balance-of-payments reasons should take the form of a uniform percentage price differential.

APPENDIX

This appendix sets out a formal model for analyzing the effects of discriminatory government purchasing policy, first for the case in which an imported good is essentially identical to its domestic counterpart, and second for the case in which imports and their domestic competitors are imperfectly substitutable. The procedures underlying an attempt to estimate the actual effects of U.S. government procurement policy from 1963 data are outlined in greater detail than in the text of this paper.

A1. Introduction: Two Types of Discrimination in Government Purchasing

The United States is unique in so far as it has systematically spelled out a set of price differentials for government purchasing agents to use in determining whether a foreign or domestic source of supply is preferable. It is only when the domestic price exceeds the foreign price by more than the differential that the agent can turn to imports.

A much more prevalent and universal sort of discrimination, however, has nothing to do with prices. It ranges from tacit admission on the part of governments that "unofficial policy is to discourage use of foreign goods," through selective and single-tender bidding schemes, through residence requirement, technical and financial specifications, and foreign-content ceilings on successful bids, and ultimately to a simple ban on foreign purchases of any kind.[1] Among its other effects, this type of discrimination undoubtedly reduces the purchasing agent's responsiveness to the price of foreign goods. It may also make foreign goods appear less substitutable for domestic goods than they appear to the private sector. And, finally, this indirect form of discrimination is strengthened by the subtle implication that it is unpatriotic for a government to buy from a foreign country.

In what follows, we will consider both discrimination on the basis of price (price favoritism) and the more informal discrimination through other means (general favoritism).

A2. Discriminatory Government Procurement When Imported Goods Are Identical to Domestically-Produced Goods

When imported goods are highly substitutable for domestically-produced goods, and competitive conditions prevail, their prices will tend to converge. Any wide divergence would lead to an almost universal preference for the good whose price is lower, since their other characteristics are very similar. If the goods are identical in every way, then their prices will necessarily be equal. Under these conditions, imports of a commodity take place only when the domestic supply is insufficient to meet the total demand.

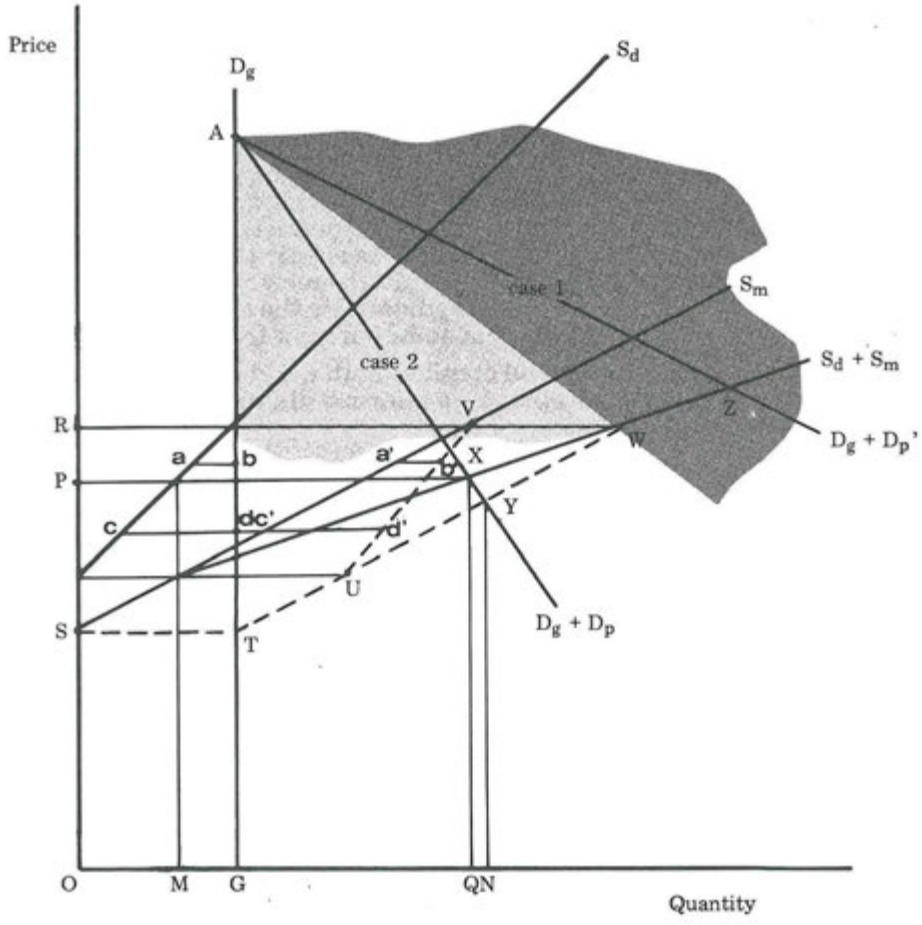
[1] See Robert E. Baldwin, *Non-tariff Distortions of International Trade* (Washington: Brookings Institution, 1970), pp. 58-70 for an outline of bidding procedures in a number of countries. See Norman S. Fieleke, "The Buy-American Policy of the United States Government: Its Balance-of-Payments and Welfare Effects," *New England Economic Review* (Federal Reserve Bank of Boston), July/August 1969, p. 7, for a general list of discrimination of this general kind practiced by state purchasing agencies in the U.S.

Thus imports would be equal to the excess demand for the good over domestic supply. This can be summarized graphically, as in Figure A1, where

D_g = total government demand for the good (assumed unresponsive to price);
$D_g + D_p$ or $D_g + D_p'$ = total government and private demand for the good;
S_d = domestic supply of the good;
S_m = supply of imports;
$S_d + S_m$ = total supply.

Figure A1

The Effects of a Ban on Government Imports When Domestically-Produced Goods and Imports Are Identical



When $D_g + D_p$ is the appropriate total demand curve, the equilibrium price is determined to be OP. At this price, total demand (OQ) exceeds domestic supply (OM) by the distance MQ. This excess demand is satisfied by imports.

Let us now impose a discriminatory government purchasing policy. Initially, because it is easier to work with, let us assume that the policy is one of general (non-price) favoritism, and that discrimination is total. That is, imports of the government are banned.

The important conclusion from this case is that under the most likely set of assumptions, absolutely *nothing* will change as a result of the discriminatory policy — neither total imports, nor prices, nor total government expenditure will be affected. The explanation for this paradoxical conclusion highlights an important feature of government discrimination in purchasing even under much weaker assumptions than those of identical foreign and domestic goods: the application of this policy always produces exactly opposite results in the private sector to those it produces for the government. Specifically, for imports, although government imports fall to zero, the private sector's imports rise. To see this, consider the implications of the assumption of identical goods and its corollary that prices of imports and domestically-produced goods cannot diverge. The effort by the government to ban government imports tends to bid down the price of imports, as the supplies formerly bought by the government are thrust onto the private market. At the same time, the price of domestic substitutes will tend to be bid up as the government shifts entirely to domestic suppliers in its purchasing. But the tendency of price movements leads the private sector to exactly the opposite changes to the government — it will substitute imports for domestic goods, and will do so to exactly the extent necessary to restore equality between the two prices. In fact, under these assumptions, the government succeeds only in bidding away domestically-produced goods from the private sector, and stimulating the private sector to increase its purchases of imports by exactly the same amount as the government reduces its own purchases. The final result is that nothing happens to total imports, or to prices.

There is, however, one case in which these conclusions do not follow. In particular, if at the price ruling prior to the ban on government imports, total government demand exceeds total domestic supply, then there are both import, price, and expenditure effects of a government ban on its own imports. In this case, the additional government demand for domestically-produced goods cannot be satisfied by bidding them away from the private sector at an unchanged price — the private sector does not purchase enough domestically-produced goods to make this possible. Thus the additional government demand can only be satisfied by an expansion of domestic supply, induced by a rise in the price of domestically produced goods. Total imports will in this case fall, since the former amount of government imports must exceed the private sector's former purchases of domestic goods under these assumptions. Thus at the old prices, the government's ban effectively generates excess supply of imports to the private sector, which can only be absorbed when the import price falls. Total economy-wide imports will fall since the lower import price discourages some foreign suppliers. It should be pointed out, however, that total imports still fall by less than the amount by which government imports fall. There is still an offsetting effect in the private sector of the market. Under these assumptions, we also find that the government's total expenditures and the incomes of domestic producers are increased by the discrimination policy.

The latter case, in which a ban on government imports does in fact lead to a decline in total imports, can be depicted in Figure A1. Suppose equilibrium before the ban on government imports is determined by the intersection of the total demand curve $D_g + D_p$ and the total supply curve $S_d + S_m$ at point X. At the ruling price (OP), domestic supply (OM) is insufficient to satisfy total government demand (OG). When a ban on government imports is imposed, this characteristic will cause the price of the domestic good to be bid up to the point where, finally, domestic supply *is* sufficient to meet government demand, at the price OR. The implication is that at prices below OR the private sector is supplied entirely by imports. To find the import supply (and hence the total supply) to the private sector in the presence of discrimination, we must add to the old import supply curve what the government *would* have imported at prices lower than OR. Foregone government imports are indicated by distances such as ab, cd, and ST, and these must be added horizontally to the old import supply curve (SVS_m) in order to generate the new one ($STUVS_m$). (Note that ab = a'b' and cd = c'd'.) Since the new import supply curve represents total supply to the private sector, and the old domestic supply curve represents total supply to the government sector, the two curves can be horizontally summed to determine the new total supply curve. This new total supply curve is STUYWZ. Its intersection with the total demand curve at Y determines the new import price in the presence of discrimination (NY), which is lower than the import price in the absence of discrimination (QX or OP). Imports will have therefore fallen (from MQ to GN). Domestic price will be higher (OR), and the government's demand will be satisfied solely by domestic supply.

Any total demand curve such as $D_g + D_p$, which begins at A and falls within the lightly shaded area labelled case 2, will imply a successful discrimination policy via a ban on government imports. This is because the equilibrium prices determined by all curves in this area are such that government demand exceeds the available domestic supply. For any total demand curve such as $D_g + D_p$', which begins as A and falls within the darkly-shaded area labelled case 1, domestic supply *is* sufficient to satisfy government demand at the price ruling prior to discrimination. In this case, a ban on government imports will be a failure in reducing total imports of the economy, as outlined above. This conclusion is demonstrated graphically in Figure A1 by the fact that the intersection of the total demand and total supply curves at Z is invariant to any of the shifts in the curves as a result of the policy, all which shifts take place to the southwest of Z.

Now let us assume that the discriminatory government purchasing policy takes the form of granting a statutory price preference (price favoritism) to domestic producers. Imports in this case are not entirely banned, but our conclusions are very similar to those for the more extreme policy. In particular, the same rule applies in determining whether or not the price preference policy will be to any degree successful: if total government demand falls short of total domestic supply at the price ruling prior to discrimination, the policy will have no effects on any aggregate quantity or price. It is only when government demand exceeds total domestic supply at the non-discrimination price that the policy will reduce imports and the price of imports, and raise price and output of domestic goods. Even here, however, the policy reduces total imports to a smaller degree than it reduces government imports, so that if policymakers do not take into account the stimulus the policy gives to private imports, they overstate its effectiveness.

These points can be demonstrated in Figure A2. Before the price preference policy is introduced, suppose equilibrium is determined by the intersection of the total demand curve $D_g + D_p$ and the total supply curve $S_d + S_m$ at point X. At the ruling price (OP), domestic supply (OM) is insufficient to satisfy total government demand (OG). Suppose now that the price preference toward domestic suppliers is introduced in government purchasing. Specifically, unless domestic price exceeds the import price by more than 100 (JI/OI) percent, the government is prohibited from importing the good. Government demand will obviously be shifted toward domestically-produced goods, and this can be depicted by observing that the perceived domestic supply curve facing the government is shifted down over a portion of the curve by the amount of the preference. The perceived domestic supply curve facing the government thus shifts from IS_d to $JKLS_d$. Under this policy, the government will again appropriate all domestic production for itself, and finding it insufficient for its total demand, there will be upward pressure on the price of domestic goods. The private sector will be left entirely dependent on imports, but it will be aided by the fact that all of the government's former purchases of imports become supply to the private sector. Foregone government imports are indicated by distances such as ab and cd, and these must be added horizontally to the old import supply curve (SVS_m) to generate the new one ($STUEVS_m$). (Again ab = a'b' and cd = c'd'). Since the new import supply curve represents total supply to the private sector, and the old domestic supply curve represents actual (as opposed to perceived) domestic supply to the government sector, the two curves can be horizontally summed to determine the new total supply curve. This new total supply curve is STUYFWZ. Its intersection with the total demand curve at Y determines the new import price in the presence of discrimination (NY), which is lower than the import price in the absence of discrimination (QX or OP). Imports will have therefore fallen (from MQ to GN). Domestic price will be higher than the new import price by the exact amount of the preference, and the government will continue to import a certain quantity of goods despite the discrimination.[2]

Any total demand such as $D_g + D_p$, which begins as A and falls within the lightly shaded area labelled case 2, will imply a successful government discrimination policy via price preference. By contrast, for any total demand curve such as $D_g + D_p'$, which begins at A and falls within the darkly shaded area labelled case 1, domestic supply *is* sufficient to satisfy government demand at the price ruling prior to discrimination. In this case, price preference for domestic producers in government purchasing will be a failure in its aim to reduce total imports of the economy. This conclusion is demonstrated graphically in Figure A2 by the fact that the intersection of the total demand and total supply curves at Z is invariant to any of the shifts in the curves as a result of policy, all such shifts taking place to the south-west of Z.

For discrimination via price preference, however, there is one intermediate case which has all the characteristics of case 2 — total imports

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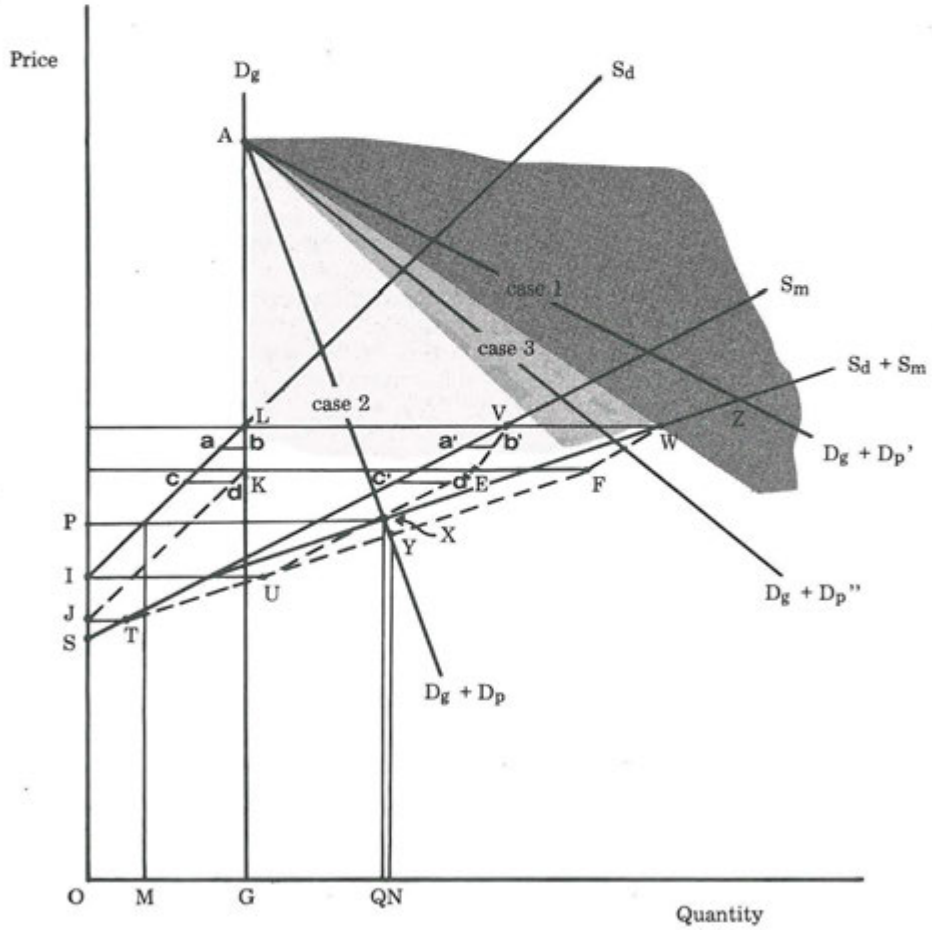
[2] If the domestic price were higher than the new import price by *more* than the preference, the government would import more and buy less from domestic producers, thus bidding it back again. If the domestic price were higher than the new import price by *less* than the preference, as long as the government's demand is not fully satisfied by domestic producers, there will be an incentive for the government to buy more from domestic producers and less from importers. This will again restore the price differential to the policy differential.

fall, prices change, etc. — but which differs in so far as government imports *do* go to zero, and the domestic price after the price preference is imposed exceeds the new import price by something *less* than the full amount of the preference. This case arises for total demand curves such as $D_g + D_p$", which begin at A and fall within the medium-shaded area labelled case 3.

Figure A2
The Effects of a Price Preference Granted to Domestic Producers in Government Purchasing When Domestically-Produced Goods and Imports Are Identical



A3. Discriminatory Government Procurement when Imported and Domestically-Produced Goods Are Imperfectly Substitutable

When imports and domestically-produced goods are imperfectly substitutable, it is notable that many of the firm conclusions derived for the case of identical goods are still true as tendencies. To the extent that there is any degree of substitutability, prices (and therefore quantities) are interdependent. And it will still be true that government discrimination in the form of either general or price favoritism tends to lead to offsetting effects in the private sector. Import prices tend to fall, and private imports tend to expand. Discrimination in government procurement policy is never as favorable to the aggregates as it may seem in a simple analysis.

The approach in this section will be algebraic as opposed to graphical, and only general favoritism, not price favoritism, will be considered. The reason is that the latter is extremely hard to work with in analytic fashion. (Since prices can differ for imperfectly substitutable goods, it requires knowledge of when and whether the import and domestic prices do in fact differ by more than the statutory differential.)

We postulate the following model:

(A1) $D_1 = f(p, p^m)$,

(A2) $D_1^m = f^m(p, p^m)$,

(A3) $D_2 = g(p,p^m) + \alpha p^m g^m(p,p^m)/p$,

(A4) $D_2^m = (1-\alpha) \cdot g^m(p,p^m)$

(A5) $S = h(p)$,

(A6) $S^m = h^m(p^m)$,

(A7) $D = D_1 + D_2$,

(A8) $D^m = D_1^m + D_2^m$,

(A9) $D = S$,

(A10) $D^m = S^m$,

where

D_1, D_1^m = the private sector's (1's) demand for domestically-produced goods and imports, respectively.

D_2, D_2^m = the government's (2's) demand for domestically-produced goods and imports, respectively;

S, S^m = total supplies of domestically-produced goods and imports, respectively;

D, D^m = total demand for domestically-produced goods and imports, respectively;

p, p^m = prices of domestically-produced goods and imports, respectively;

α = a discrimination parameter defined below.

Equations (A1) and (A2) are the private sector's demand functions for the two goods in the system. Since the goods are substitutes, both prices

appear in each equation. Equations (A3) and (A4) are the government's demand equations. The term a represents a discrimination parameter for the sort of discrimination described above as "general favoritism". Specifically, in equation (A4) above, if $a = 1$, government imports are banned and are, consequently, zero. If $a = .50$, discrimination is such as to reduce government imports in the absence of discrimination by one half. There is also a discrimination effect on equation (A3), where it is assumed that whatever the decline in expenditure on imports because of discrimination ($= \$a p^m g^m( )$), it is reapplied to the purchase of domestic substitutes: $\$a p^m g^m( )$ will buy $a p^m g^m ( ) / p$ units of the domestic good. This type of interdependence between equations (A3) and (A4) is believed to be consistent with the observation that, given a set of prices, the government has a certain budgeted expenditure which cannot be exceeded, and which will not be left unspent, given the dynamics of administration. Equations (A5) and (A6) represent supply equations. It is notable that all the supply and demand equations are specific to a particular good, and all are partial-equilibrium. Equations (A7) and (A8) are definitions, and equations (A9) and (A10) are equilibrium conditions.

It is a straightforward, although tedious, exercise to determine the effects of a change in the degree of total discrimination (a) on total imports ($p^m D^m$) and other variables in the system. To be specific, in the case of imports,[3]

$$\text{(All)}\quad \frac{d(p^m D^m)}{p^m D^m} = (1 - N_1^m R_1^m - N_2^m R_2^m)dp^m + (\gamma_1^m R_1^m + \gamma_2^m R_2^m)dp - \left(\frac{R_2^m}{1-a}\right)da,$$

where

$$dp^m = \left(-\frac{1}{\triangle}\right)\left(\frac{R_2^m}{1-a}\right)\left\{ [\epsilon + N_1 R_1 + N_2 R_2 \left(1 - \frac{aV_2}{1-a}\right)] \right.$$

$$\left. - V[\gamma_1^m R_1^m + (\gamma_2^m - a)\left(\frac{R_2^m}{1-a}\right)] \right\} da,$$

and where

$$dp = \left(\frac{1}{\triangle}\right)\left(\frac{R_2^m}{1-a}\right)\left\{ V[\epsilon^m + N_1^m R_1^m + (N_2^m - a)\left(\frac{R_2^m}{1-a}\right)] \right.$$

$$\left. - [\gamma_1 R_1 + \gamma_2 R_2 \left(1 - \frac{aV_2}{1-a}\right)] \right\} da,$$

and where

$$\triangle = [\epsilon + N_1 R_1 + N_2 R_2 (1 - \frac{aV_2}{1-a}) + (1-\gamma_2^m)\left(\frac{aVR_2^m}{1-a}\right)].$$

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[3] In the derivation of equation (All), quantity units have been assumed to be defined in such a way that the initial value of both prices equals one. This in no way affects the generality of the results.

$$\cdot [\epsilon^m + N_1^m R_1^m + N_2^m R_2^m] - [\gamma_1 R_1 + \gamma_2 R_2 (1 - \frac{a V_2}{1-a})$$

$$+ (1 - N_2^m)(\frac{a V R_2^m}{1-a})] \cdot [\gamma_1^m R_1^m + \gamma_2^m R_2^m],$$

and where the variables are defined as follows:

$\frac{d(p^m D^m)}{p^m D^m}$ = the proportional change in total imports as a result of the change in discrimination policy (da);

dp, dp^m = the change in the prices of domestic goods and imports, respectively, as a result of the change in discrimination policy (da);

ϵ, ϵ^m = supply elasticities of domestically-produced goods and imports, respectively;

N_1, N_1^m, N_2, N_2^m = direct demand elasticities of the private sector (subscript 1) and the government (subscript 2) for domestically-produced goods and imports, respectively (defined positively);

γ_1, γ_1^m, γ_2, γ_2^m = cross-price elasticities of the private sector (subscript 1) and the government (subscript 2) for domestically-produced goods and imports, respectively;

R's represent ratios of each sector's demand to total demand, meaning $R_1 = D_1/D$, $R_1^m = D_1^m/D^m$, $R_2 = D_2/D$, $R_2^m = D_2^m/D^m$;

V's represent value ratios of import demand to domestic-good demand, meaning $V = pmDm/pD$, $V_2 = pmD_2^m/pD_2$.

Although little else can be said about the very complex equation (All), choices of reasonable values for the parameters assure a decline in imports. The expression does, however, provide a useful beginning for the estimation of the actual effects of U.S. discrimination in government procurement. Although the elasticity parameters are not directly observable, the share ratios (R's and V's) are. And the available data can also be used to approximate an initial value for a, the discrimination parameter, which is not directly observable either. These procedures are outlines in the next section.

A4. The Quantitative Effects of Discrimination in U.S. Government Purchasing on Total U.S. Imports

This section outlines the methods and detailed results from a simulation study of the effects of U.S. government procurement policy on imports.

The study was based on equation (All) above, and utilized data from the 1963 Input-Output table, broken down into broad commodity classes.[4] For each commodity class, the data consisted of the 1963 values of the private sector's domestic purchases and imports, and the government's domestic purchases and imports ($_pD_1$, $_p{}^mD_1^m$, $_pD_2$, $_p{}^mD_2^m$, respectively).[5] These four numbers alone were judged capable of yielding an initial level of the unobserved discrimination parameter a, and were used for that purpose.[6]

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[4] U.S. Department of Commerce, *Input-Output Structure of the U.S. Economy: 1963.* The breakdown of actual government imports by commodity class was, however, furnished directly by the Department of Commerce. The commodity groupings were restricted to manufactures in the Standard Industrial Classification, since most other types of goods (agricultural and mineral) are not subject to government discrimination in purchasing. On the same grounds, petroleum (S.I.C. 29) was excluded from other manufactures. The commodity groups are listed below, where the first set of brackets enclose the input-output industry designations entering the group and the second set of brackets enclose the S.I.C. industry designations:
ordnance and accessories (13) (19),
non-durable manufactures (14-19, 24-29, 31-34) (20-23, 26-28, 30-31),
lumber, wood, stone, clay, glass products (20-23, 35-36) (24-25, 32),
primary and fabricated metal products (37-42) (33-34)
non-electrical machinery (43-52) (35)
electrical machinery (53-58) (36)
transportation equipment (59-61) (37),
instruments and miscellaneous (62-64) (38-39).

[5] In each commodity group, the figure for government imports was entered directly as D_2^m. D_2 consisted of federal government purchases from the column with that label in the input-output table, *less* D_2^m. D_1^m consisted of transferred imports from row 80B of the input-output table *less* D_2^m. And finally, D_1 consisted of the sum of intermediate output, personal consumption expenditure, gross private fixed capital formation and net inventory change from the input-output table, *less* D_1^m.

[6] The estimate of a was obtained by the following reasoning: in the absence of discrimination, it seems a reasonable hypothesis that the government would import about the same proportion of a selected commodity as the private sector. That is to say, on a commodity by-commodity basis, the government's average propensity to import would be identical to that of the private sector when $a = 0$. Admission of this hypothesis can be used in the following way to obtain an estimate of the initial or present degree of discrimination. Equation (A4) above expresses a proportional relation between actual government imports, D_2^m, and hypothetical government imports in the absence of discrimination, $_g{}^m$ ( ). Multiplying through equation (A4) by $_p{}^m$ yields a relation between the actual and hypothetical *values* of these transactions (say actual value = X_2^m and hypothetical value = $\bar{X}_2^m$). This relation appears below as equation (A12). Similarly, equation (A3) above expresses a proportional relation between actual government purchases from the domestic sector, D_2, and hypothetical purchases in the absence of discrimination, $_g$ ( ). Similarly, multiplying through equation (A3) by $_p$ yields a relation between actual and hypothetical *values* of these transactions. This relation appears below as equation (A13).

(cont'd on p. 261)

The data for D_1, D_1^m, D_2, and D_2^m were by definition sufficient to yield values for the ratios R_1, R_1^m, R_2, R_2^m, V, and V_2. Thus in terms of equation (All), the only parameters remaining to be specified were the supply and demand elasticities. These were arbitrarily chosen on the basis of *a priori* expectations about reasonable values for each particular commodity classification.

Having established an initial level of discrimination and knowing the value of total imports at that particular level, it is a comparatively simple matter to plug the actual and assumed values of variables into equation (All), and read out the changes in total imports which would take place given a change in a. In fact, the procedure followed was to determine the changes in D_1, D_1^m, D_2, and D_2^m which would come about from a 0.10 increase or decrease in a from its original value, then to use these changes to establish *new* values of D_1, D_1^m, D_2, and D_2^m, and therefore also new values for all the share ratios (R's and V's). These new values, in addition to the increased or decreased value of a then provided the new raw data to plug into equation (All) a second time. With the resultant second set of changes,

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(Cont'd from p. 260)

(A12) $$X_2^m = (1 - a)\bar{X}_2^m$$

(A13) $$X_2 = \dot{X}_2 + a\bar{X}_2^m$$

Returning to the hypothesized equality between average propensities to import in the absence of discrimination, it implies algebraically, that

$$\frac{\bar{X}_1^m}{\dot{X}_1} = \frac{\bar{X}_2^m}{\dot{X}_2}.$$

However, for a country like the U.S., the *hypothetical* ratio of private imports to domestic purchases is sure to be approximated by the *actual* ratio, because of the very large size of domestic production compared to imports, and the comparatively large private sector compared to the government sector. This suggests the approximate equality of equation (A14):

(A14) $$\frac{X_1^m}{X_1} = \frac{\bar{X}_2^m}{\dot{X}_2}$$

Equations (A12), (A13), and (A14) are then a system of three equations in three unknowns (the two hypothetical values $\bar{X}_2^m$ and $\dot{X}_2$, and the actual degree of discrimination a). Thus a solution for the present level of discrimination is obtainable by solving the three-equation system. a becomes a function of known quantities:

$$a = \frac{X_2/X_2^m - X_1/X_1^m}{1 + X_2/X_2^m}.$$

Use of the approximate equality (A14) assures that this is a slight over-estimate of a, and in the actual estimation reported above, the estimated a was rounded off in a downward direction to the nearest 0.Z5, where the digit Z varied between 0 and 9.

the levels could be revised a second time for a new value of the discrimination parameter, and the whole process repeated. In addition, at each iteration, the values of the assumed elasticities of demand of the government were raised when a was being decreased, and lowered when a was being increased. This was consistent with the notion that increasing general favoritism to domestic producers also lowers the price sensitivity of the government purchasing agent.

What emerges from this procedure is a "hypothetical history" of government discrimination against imports for each commodity class — what the value of total imports in 1963 would have been if the government had engaged in any degree of discrimination from none at all to total exclusion of imports in government purchases. On the basis of one observation on actual data, the values of all variables in the system were calculated for $a = 0$, $a = 1$, and $a = 0.05$ to $a = 0.95$ by 0.10 intervals. The process described is essentially a numerical approximation to the result obtained from integration of the right hand side of equation (A11) from $a = 0$ to $a = 1$.

Table A1 records the findings of the simulation with respect to total imports for (i) the initial value of a (columns (2) and (4)), (ii) no discrimination ($a = 0$, column (5)), and (iii) a ban on government imports ($a = 1$, column (6)).[7]

Two sets of hypothetical figures are given in Table A1, the first for relatively short-run (low) values of supply elasticities, and the second for relatively long-run (high) values. From the totals row it can be determined that the discriminatory U.S. procurement policy of 1963 actually "saved" $76 million dollars of imports under the short-run assumptions, (8169 - 8093 = 76), or $110 million dollars of imports under the long-run assumptions (8203 - 8093). The long-run figure would be appropriate if it were believed that both foreign and domestic suppliers had had sufficient time to adjust to the program of discrimination, and if it was known that there had been no recent substantial changes in the program's implementation.

The extent to which 1963 imports were decreased as a result of discrimination in government purchasing is notably small under any assumptions. And Table A1 also demonstrates that there is little to be gained from further discrimination. An outright ban on all government imports would reduce total imports only another $36 million in the short-run (8093 - 8057), or $54 million in the long-run (8093 - 8039). In either case, it is notable that banning the remaining $61 million (from column (3)) of government imports does not reduce *total* imports by this full amount. As has been discussed at length above, a policy of discrimination against imports in government purchasing actually discriminates in favor of imports to the private sector by lowering the price of imports.

The small magnitude of actual 1963 government imports ($61 million) may seem surprising. But it is due in part to the exclusions of certain commodities and types of purchases in Table A1, and it is due in great part to the substantial degree of *actual* discrimination against imports which reduces their importance in government purchases. The high levels of actual government discrimination are clear from column (4).

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[7] More detailed results for other variables than total imports and for intermediate degrees of discrimination (values of a) are available from the authors on request, as are the assumed values of various elasticity parameters underlying Table A1.

TABLE A1
Actual and Hypothetical Values of Imports and the Degree of Discrimination in Government Purchasing: 1963

(1) Commodity Group[a]	(2) Actual Total Imports	(3) Actual Government Imports[b]	(4) Actual Degree of Discrimination (a)	(5) Total Imports If No Discrimination ($a = 0$)[c]	(6) Total Imports If Government Imports Banned ($a = 1$)[c]
	millions of dollars				
Ordnance	18	2	0.95-1.00	47 52	16 16
Non-durables	3768	0.3	0.95-1.00	3769 3771	3768 3768
Lumber, wood, stone, etc.	680	0.1	0.95-1.00	680 681	680 680
Metal products	2059	1	0.75-0.85	2060 2062	2059 2058
Non-electric machinery	469	6	0.65-0.75	475 479	466 464
Electric machinery	420	25	0.65-0.75	445 460	407 399
Transport equipment	232	25	0.35-0.45	242 245	215 209
Instruments, miscellaneous	447	1	0.95-1.00	451 454	446 446
Total[d]	8093	61	—	8169	8057

[a] See footnote 4 of this appendix for a detailed outline of the composition of each commodity group.

[b] Not including either the specific commodities mentioned in footnote 4 or *any* Department of Defense purchases for use abroad. The latter exclusion is forced by the inability to get a commodity breakdown on such purchases, and totals over $2 billion.

[c] Two numbers appear for each commodity group. The first assumes short-run values for supply elasticities (2 and 1, respectively, for domestic goods and imports). The second assumes long-run values for supply elasticities (20 and 10, respectively).

[d] Detail may not add to total because of rounding.

COMMENTS BY PROFESSOR H. T. PATRICK

In regard to Professor Baldwin and Richardson's statement that NTBs should be removed or moderated with exchange rate realignment, Professor Patrick wondered whether there were criteria or circumstances when NTBs are beneficial or necessary. He noted that NTBs are a second-best way of solving some domestic industrial problems, retarding structural adjustment and perpetuating the situation of a new generation of workers spending their lives in marginal industries. For example, protecting black industry in the U.S. this way would be very inefficient. Similarly, although Professor Komiya said that Japan merely wishes to use NTBs to buy time for adjustment in the leather industry, Professor Patrick suggested the Japanese government is simply using this as an excuse to keep these workers as second-class citizens in the leather industry and to avoid integrating them into the fuller aspects of Japanese society.

Professor Patrick wondered how important Professors Baldwin and Richardson's estimates of 100 million dollars difference due to government procurement policies would be for specific industries. He was concerned about their method of using existing imports by the private sector as a measure of what could occur, for it might well be that many government-used goods, such as military ordinance, are not used privately at all. He suggested using this model for Canada, Australia and Japan where the imports of military equipment may be much more important and where it would be useful to know the opportunity cost of producing military equipment domestically.

Professor Patrick agreed that their policy proposals including a code of fair practices and public bidding were good ideas. He noted that Japan buys almost nothing from abroad and even with respect to domestic producers the government maintains a selected list.

In reply to comments on his paper, Professor Komiya said he had used unpublished, non-official government sources. One group of sources was the complaints by GATT members, presented to GATT, against Japan's non-tariff barriers. A second group was the special talks between the U.S. and Japan on these special problems and for these talks, complaints and information were collected from American businessmen. With regard to administrative guidance, he said there were genuine complaints from the U.S. side, but the only concrete case he could identify in the manufacturing sector was the power generator case. He did note that in agriculture non-tariff barriers were much more important than in manufacturing. He also mentioned that the U.S. was very eager to initiate the above U.S.-Japan talks on these matters, but the U.S. requested the talks be stopped after two or three meetings because it was soon discovered that trade barriers were much greater on the U.S. side than the Japanese.

Professor Komiya said that although the quantitative importance of NTBs is a very difficult subject, a Japanese government official has made some estimates of trade reduction due to these trade barriers. Although these estimates would naturally be minimized, NTBs accounted for a reduction of about 1.5 - 2.0 billion dollars per year and tariffs accounted for a reduction of about 2.5 - 3.0 billion dollars.

With regard to the computer industry, Professor Komiya said it produced general types of computers and that, besides residual import restrictions, the government provided low interest credit and financing for R and D projects. While it might be more efficient to have just one company, in Japan it is difficult to merge four companies and even though this is not the best policy, he said at least the industry was growing. With respect to tariffs and quotas on primary metals, he said that this was not a progressive policy at all and that it served only to protect inefficient industry.

A participant from an international institution said that GATT permits a certain amount of state trading because of the provisional character of part 2 of GATT which permits other than GATT provisions in trade arrangements if they have been part of the country's legislation prior to agreement in 1948. Most countries had state trading arrangements in agriculture before 1948. Professor Komiya replied that his information was different and that quite a few of the state trading arrangements were instituted after 1948. Thus, if the above participant is correct, then the Japanese arrangements are in conflict with GATT. The above participant also emphasized that people ought to get away from the idea that anything not conforming to GATT is bad because, while it is a good forum for discussion, many of its regulations need revision.

A U.S. participant regretted that there were no substantial estimates of the quantitative effects of NTBs. In reference to the U.S.-Japan talks mentioned, he said his impression was that the U.S. government had not done any study of the subject beforehand, but rather collected *ad hoc* complaints and then relied upon Japan and the GATT for further information. An example of such complaints was given by a member of the Canadian business community who was present at this session. He said in regard to the Japanese list of items which are not liberalized that there are many

examples of items not on the list which cannot be sold in Japan even though such items are competitive in price, delivery and so on. The U.S. participant continued that he was concerned about the conflict between reality and image concerning administrative guidance. He said Japan is getting the Japan, Inc. image that there is such government-business cooperation that a special set of rules are needed to deal with Japan, just as with the Soviet Union. Hard data are needed to evaluate the many individual stories supporting the image because saying things like there are many foreign trading firms does not resolve these issues when 60 per cent of Japan's imports are handled by ten firms and the remaining firms handle highly specialized imports. The Ministry of Trade and Industry, which is very specialized itself, can talk to the ten small firms that import a particular machine just as easily as to the ten large firms. One way to get data is by surveying American exporters and foreign chambers of commerce in Japan about their problems at both the importing and selling levels.

A participant from an international institution drew a moral from these discussions. Upon first entering the exporting of manufactures in the 1920s and 1930s Japan encountered the types of restrictions that have been discussed on the part of the then developed countries. Australia was one of the first to pass legislation — in 1931 — which aimed at the diversion of imports away from Japan. Moreover, all colonial countries took steps to keep Japanese imports out of their colonies. These were not inconsiderable factors in Japan's entry into World War II, and thus, from these examples, it is not surprising Japan got into the frame of mind of strictly regulating imports. This participant said that, on the whole, this policy has worked very well for Japan. Similarly, it can be argued, for several of the developing countries with a population of more than 40 million and a reasonably large domestic market and in a world of trade barriers, that the way to develop is to follow the Japanese pattern and play the game by the protectionist rules set by the developed countries and Japan. However, if the developing country plays the game badly, it will get into a terrible mess since it will not know where its resources are going. Also, the Japanese problem is not only that it is difficult to dismantle barriers but also that it is difficult to dismantle the protectionist frame of mind which is now counter-productive for Japan. Another participant commented that many countries do not have the social structure or administrative capacity to play the protectionist game without losing.

One of the assumptions on which Professor Baldwin and Richardson's analysis rested was that, for individual commodities, if there were no discrimination, the average propensity of the government to import would be the same as the private sector's propensity. Professor Richardson agreed with Professor Patrick's criticism of this assumption that at a high level of aggregation the distribution of the government's is not known and thus that this is a strong assumption. Different results would be obtained with different levels of aggregation, however, experiments with higher levels of aggregation than the 8 or 9 categories in the paper did not give substantially different results, thus the results of the paper are likely ballpark figures.

One participant was interested in the analogy between the small price tag on government procurement policies and the small price the Japanese put on some of their practices and wondered why there was so much concern about apparently small problems. Professor Richardson said he was not sure, perhaps it was a matter of psychology in the way small cases get blown out of proportion.

A Japanese participant wondered if exchange rate realignment would cure all the problems with the United States' balance of payments. He suggested that some types of structural problems, such as the U.S. automotive industry being 15 to 20 years obsolete compared to the Japanese or West German industries, could not be remedied by exchange rate adjustment. He said this type of problem required instead new investment which was why Japan was able to catch up in these industries. However, it was replied that during the Kennedy-Round, the U.S. wanted to lower all trade barriers and that the demand for trade barriers had only grown very much in the last three or four years. It was suggested that this was due to the U.S. currency being out of line, and to the fact that structural problems are much more difficult to solve when a country's currency is out of line.

Finally, Professor Richardson emphasized that the longer the surcharge stays, the more people think that it is part of normal affairs. A further problem is that part of the ultimate bargain is a resetting of parities, but when the surcharge comes off, the exchange rates will be back into disequilibrium, even if the correct equilibrium exchange rates were guessed with the surcharge.

Policy Approaches to the Liberalization of Pacific Trade

TRADE LIBERALIZATION AND THE ECONOMIC DEVELOPMENT OF THE PACIFIC BASIN: THE NEED FOR COOPERATION

by

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There are many proposals for bringing about trade liberalization, within the Pacific Basin, and in the world trading system as a whole. One could analyze each of these in terms of their likely technical economic effects, and make recommendations based upon their relative economic efficiency as instruments of liberalization. Such an approach would lean heavily on some basic theoretical propositions, and some kind of complex model. Another way in which to contemplate alternatives is to consider the major economic and political trends, and the restructuring of trade, investment, and production patterns which might result from them. Methods of liberalizing trade could then be evaluated in terms of their practicality, and the degree to which they cope with the underlying forces. The latter approach is used in this paper.

The Pacific Basin countries are undergoing a structural transformation in their relations with each other, and with the rest of the world. The forces at work are numerous.

Trade policies in Europe and in the United States have a major effect on the outlook for trade and investment in all of the countries of the region. In Europe, the enlargement of the Community will give further impetus to the reorientation of the economies of Australia, New Zealand, Canada, and others. At first, the impact of enlargement will be limited to further consolidation of the European Common Agricultural Policy (CAP) with major consequences for cereals and dairy exports. The CAP operates to stimulate production and encourage aggressive export subsidization, in addition to restricting imports rather severely. There will be years in which European Community imports are relatively high, as they were in 1970-71, when Community crop conditions were poor. On the whole, however, imports of products covered by the CAP will not perform well, and are likely to continue to decrease. The degree of European self-sufficiency is likely to rise, and the upshot is very likely to be increased exportation of surpluses. While there will be good years and bad, the EC potential for exportation of most of the basic temperate commodities will act as a disruptive and price-depressing influence on markets throughout the world.

The enlargement of the European Community will require special arrangements for the EFTA countries which do not become full members of the European Community. These arrangements will probably take the form of free trade for industrial products between the Community and non-member EFTA countries. There will also be further proliferation of discriminatory Community preferential arrangements in order to accommodate the British-related Caribbean countries, Mauritius, and possibly even India and Pakistan. This will blur the limits of the Community's special preference network, which up to now has been limited to the Mediterranean and most of Africa. The new economic bloc centered on the Community will encompass about

a half of present world trade, and will have the combined political voting strength of about fifty nations in the international economic institutions. The sheer size of this Eurobloc will change the modes of operation of international institutions and rules, and affect the planning and the policies of all other countries, whether they be developed or in early stages of development.

In the United States, there is a strong resurgence of protectionism, and even a tendency towards a kind of neomercantilism. This manifests itself in *ad hoc* trade restrictions, usually in the form of so-called "voluntary" export quotas, the inability to obtain authority from Congress for trade negotiations, and the near-passage of generally restrictive trade legislation on more than one occasion, since the end of the Kennedy-Round in 1967. The shift of the American labor movement from its traditional support of liberal trade policies to its new position of favoring both controls on imports and on direct investment outflows has caused a major change in political alignments in the direction of neo-isolationism. This trend was highlighted by the unilateral character of the President's actions in August 1971 to shock the rest of the world into recognition of the need for a change in the monetary and trade mechanisms.

These developments have been building for several years. For example, the beef import quota legislation which now acts as a restraint on Australian and New Zealand exports was enacted in 1964. The pressures for textile import restrictions began even before President Kennedy took office in 1961. These pressures have continued and intensified, and have always been primarily aimed at curtailing imports from eastern Asia, as opposed to other sources from around the world. The pressures to control stainless steel flatware, or shoes, or other labor-intensive products began in the mid-60s.

Frustrations with European Community policies, intensified competition from Japan, the weak state of the domestic economy, and the chronic balance of payments deficits were added to the political frustrations over the Vietnam War, and the distribution of the economic burden of defense among the Western countries. This turning inwards has left up in the air a number of initiatives the U.S. itself had taken, or been party to. Among the recent casualties are the funding of the international development institutions such as the IDA affiliate of the World Bank and the proposed soft-loan facility of the Asian Development Bank; the multilateral untying of aid; the implementation of general tariff preferences by the U.S.; and the UN development target for development assistance at one percent of GNP, or the Pearson Commission target for official aid at 0.70 percent of GNP. As regards the latter point, even the requests for foreign aid appropriations by the Executive Branch have been going down.

The outlook for the developing countries of East and Southeast Asia, and even of South Asia, has been adversely affected by these developments. A major element in the 1970 and 1971 American policies on trade was a collision with Japan, both officially, and on the level of private business activities in the Pacific. A mood of hostility in the United States has grown rapidly, among certain important segments of the American political and economic system. The recent sharp rise in protectionist sentiment on specific trade matters is a reaction to these developments. First, the export successes of Japan, Korea, Taiwan and Hong Kong have generated strong reactions to the consequent import penetration. Second, some American companies have built processing or assembly facilities in this area, to bring in products formerly produced in the United States. The major examples are in the electrical and electronics industry, especially in the recent shift of all radios and much

of the television production to Eastern Asia. Third, American manufacturers discovered that European countries have maintained a number of formal and informal controls on imports from Eastern Asia on what is essentially a discriminatory basis. This is interpreted as a major cause of the concentration on the U.S. market for the exports of manufactures from Eastern Asia.

Perhaps it is worth adding that the economic consequences of the winding down of the Vietnam war, and the shift in the American role implied in the Guam Doctrine, have not been given much attention in planning for the future. The idea of providing military assistance, particularly in the form of equipment and arms, has been subject to discussion. This is what has so far been meant by "supporting the initiatives of other nations." The notion that there should be an economic design in place of the military role, which would provide development assistance and promote trade and investment in the area, has not been given serious consideration, at least thus far. What I have called elsewhere "the other half of the Guam Doctrine" is missing.[1]

Also at work are a number of other forces which will bring about structural change. Most important among these is the growth and evolution of the Japanese economy, and its relations with the rest of the world. As the other papers in this and past Pacific Trade and Development conferences make clear, the Japanese demand for exports of the region has a strong effect on the trade and production pattern of the area. This area is a large market, second only to the U.S. More important in the long run, however, is the labor, raw materials, and plant sites which the region provides. On the labor side, the shortage of manpower in Japan in relation to the size and growth of the Japanese economy dictates expansion of the Japanese industrialization base by location of plants outside Japan, in labor surplus countries. The demand for raw materials from various parts of the Pacific Basin, and from other parts of the world, will continue to rise. This will tend to cause movement of Japanese investment into supply areas. The pollution problem in Japan, in combination with the scarcity and cost of new sites for industrialization in Japan, at least in presently suitable locations, creates an additional incentive to move abroad, at least with the expansion of industries beyond their present size.

In the past, while the share of Japan's total world exports going to this area has held steady, the share of Japan's total imports from this area has been going down in recent years (in spite of the fact that the absolute level has more than doubled, e.g., from $718 million in 1960 to $1.5 billion in 1968).

THE EASTERN ASIAN SHARE OF JAPAN'S TRADE
(Eastern Asian Developing Countries from Burma Eastwards)

	Percentage of Japan's Total Trade	
	1960	1968
Japan's Exports	24.7	24.5
Japan's Imports	16.0	12.6

[1] "Coming Trade Wars? Neomercantilism and Foreign Policy," *Foreign Policy*, winter, 1970-71.

Viewed from the vantage point of the developing countries of Eastern Asia, the picture varies from country to country. Indonesia, Philippines, and Thailand are becoming increasingly dependent upon the Japanese market for their exports; while Taiwan, Korea, and Malaysia show signs of becoming less dependent upon Japan in terms of the share of exports of that destination. For the group as a whole, over one-fifth of their total exports went to Japan in 1968.

The composition of Japan's trade with this area is well known: Southeast Asia primarily supplies raw materials and takes finished goods; while Taiwan, Korea, and Hong Kong are moving into manufactures and semi-manufactures for the Japanese market. These latter three countries now import more machinery from Japan than they export light industrial goods to Japan, but this balance is likely to shift fairly soon.

What lies ahead cannot be assessed without reference to the changing priorities in the Japanese economy, towards social overhead, services, and pollution control, and to the outcome of the exchange rate realignments in 1971 and subsequently. There has always been controversy about how fast Japan was likely to grow with continuing forecasts of a slowdown. This has not happened, except for brief intervals. The exchange rate change could be a new retarding-factor, as might be more restrictive Western trade policies. However, the shift to construction, services, and clean-up activities will probably mean declining import requirements as a proportion of total economic activity in Japan. Japan's so-called dependence on imports could very well decrease, except for energy sources.

On the export side, Japan can be expected to continue to enjoy high rates of growth, perhaps a little less than past expansion of double the global export growth rate, but nonetheless high. This, however, is not a crucial element in Japan's high GNP growth rate, since exports in recent years appear to have followed domestic expansion, rather than led it.

Japan's liberalization of import restrictions and direct investment outflows, and the growth of Japan's foreign aid programs, are likely to have a major impact on the Pacific, whatever the home growth rate or new exchange rate situation. Particularly in agriculture, import liberalization could have an enormous effect on the outlook for all of the producing countries of the Pacific, including the developing countries.

In agriculture, in the region, there are two major forces which are transforming the traditional pattern. The hybrid seeds of the Green Revolution and technological progress generally have enabled South Asia and parts of Southeast and East Asia to become self-sufficient, and have allowed hopes of export potential to rise. The second major force at work is the virtual self-sufficiency in rice of Japan, and Japan's potential to dump its surpluses of rice through food aid programs. This progress in production is based in many cases on inefficient farm programs. The support prices for rice in Japan are the equivalent of treble the world market price for comparable qualities. Japan thus has to follow a highly protectionist trade policy in agriculture. The support prices for grains in the developing countries is also generally high, contributing to the recent improvements in their production. The upshot is that the opportunity for selling grains to each other, or to the rest of the world, is small. The international future of rice, like all other grains, will likely be a future of high production and low prices, with exportation made difficult by self-sufficiency in other countries, by protectionist policies in the major potential markets, and by the competition of export subsidization

by some of the exporting countries. Hopes for the evolution of Southeast Asia as the "rice bowl" for the rest of Asia are probably misguided, and the real potential, so far as there is one, is higher up the protein ladder, in feed supplies at first and in ultimately the sale of meat as incomes grow.

There is a major change underway in the performance and growth of the manufacturing sector in some of the countries. The export performance of Hong Kong, Taiwan, and Korea provides a model for others. There seems to be a clear pattern of international adjustment into labor-intensive manufactures and food processing, and eventually into light engineering and consumer goods, and componentry and assembly. The latter developments are to a considerable extent tied up with the so-called internationalization of production of larger corporations in Japan and North America.

Finally, the population problem in the developing countries is increasingly manifesting itself in unemployment. The rising unemployment problem is coming at a time when labor requirements for agriculture appear to be declining, thus putting a premium on the generation of jobs by the manufacturing sectors.

This overview of the major changes underway may be too general and too simplified to provide guidance in very specific cases, but it is helpful in making broad judgments about what the trade problem is, and how we go about improving the conditions of trade. This overview also sets aside the potential role of Eastern Europe, and especially the People's Republic of China. The potential impact of these can only be matters of speculation at this juncture. China will sooner or later have the ability to export a wide range of labor-intensive manufactures. At present its capabilities are limited to such products as textiles where international competition is already keen. However, China for some time yet is mainly a matter of potential.

Against this background of structural changes we can consider the possibilities for liberalizing trade pragmatically. Perhaps the first question that might be asked is whether the introduction of generalized tariff preferences by the developed countries will open a variety of new trade opportunities and reduce the need for other forms of liberalization in the near term. My answer to this is pessimistic. The United States scheme of general preferences has not even been sent up to Congress in the form of proposed legislation, because the Executive rightly fears transformation of any trade legislation into protectionist legislation of a different character altogether. If implemented, the U.S. scheme would have safeguards against market disruption, in the form of exceptions made for "sensitive" labor-intensive products and an escape clause procedure. The latter escape procedure would probably be sought by U.S. manufacturers and workers fairly frequently, and the Tariff Commission if it followed its other recent practices would probably support snap-backs to the MFN rate often. The uncertainty generated would be high. The U.S. will probably not offer preferences to any developing country giving so-called "reverse preferences" to one or more developed countries under discriminatory preferential arrangements of the European type. This is intended to provide a long-term incentive to phase out a substantial element of the special preference arrangements, and it would in theory reduce American Congressional opposition by withholding preferences from any country which discriminated against U.S. exports. In practice, ironically, this position will probably result in perpetuation of the special preferences with the Community. The African and Mediterranean countries do benefit from the aid flows tied to their preferences, and some gain marginal benefit from the preferences themselves, whereas giving these bilateral arrangements up for the sake of

preferential access to the U.S. would not be attractive. What, after all, would they sell in the U.S.? In the long run, the U.S. may alter its position quite possibly in the direction of asking for reverse preferences on certain products for itself.

The Community general preference scheme offers certain theoretical advantages over the American scheme, looking at the whole of the developing world together. The Community would first of all not invoke a safeguard (snap-back to MFN rates) unless imports from preferred countries had reached a certain trigger level. The trigger would be observable, in theory, and therefore countries could plan more effectively. Second, the Community would place imports of a certain product from a given country back into the MFN category if that country's exports of the item exceeded one-half of the total volume allowed under the ceiling, or trigger level. This would mean that countries which became relatively strong competitors would be moved into normal competition with the developed countries, making room for the lesser developed countries to use preferences to develop a capability to export. This system in its original conception had much to say for it, and I earlier advocated that the U.S. adopt a similar system rather than face the uncertainties and diplomatic strife implicit in the American escape-clause procedure.[2]

As matters turned out, the Community went ahead with implementation of a general preference scheme in the summer of 1971 even though the U.S. was not yet ready, nor was there indication of when the U.S. might be able to take action. This apparently courageous step by the Community is not all that it seems. Based upon analysis of the specific mechanics, Professor Richard Cooper has concluded that the Community scheme as now implemented will offer almost no additional incentive to developing countries to export.[3] The tariff-quotas have been set on a base of 1968, with a low add-on allowance. The rate of growth of successful exporters is such that they will end up exceeding the tariff quotas in the initial period, or shortly thereafter. The actual mechanics will in particular block preferential access for East Asia. In defense of the new system, Community officials have stated that the quantitative threshold levels would in practice only be used as an indicator of what was taking place. Official action to invoke the safeguards would be rare, usually only in the case of the more sensitive products. This however means that there will be great uncertainty as to when the triggers might be invoked. No predictable, continuing assurance of market access would be provided. Experience has shown that complaints are made in the developed countries when imports actually make significant progress in the market. A number of complaints already suffice to bring about requests for "voluntary" restraint of exports; it will be all the more likely that complaints under a preference scheme would result in a snap-back to the MFN rate.

Since the new members of the Community, including Britain, will adopt the same scheme, and since the Japanese have initiated it as well, the result has been the creation of a complex, technically ingenious trade mechanism which gives rise to false hopes and few benefits — and which probably discriminates against East Asia. It is probably fair to say that the general preference mechanism as instituted by the Community will thus do little to end the privileged position of Africa and the Mediterranean, and other associated countries. Added to this is the fact that the "sensitive" items excluded

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[2] See my discussion of general preference schemes in my monograph, *Trade for Development*, Overseas Development Council, Washington, D.C., 1971.

[3] "The European Community's System of Generalized Tariff Preferences," unpublished paper, summer 1971.

by the U.S. proposal, and the "sensitive" items in the Community framework, will normally be labor-intensive products from East Asia.

Any form of liberalization through the device of general preferences thus has to take into account these practical problems of safeguards, of providing opportunity for the least developed while restraining the most competitive from taking the lion's share, and at the same time ensuring some improvement of the opportunities of exports of manufactures from Asia to Europe. Reconciling these problems in one scheme is very difficult, and too much hope cannot therefore be placed on such a scheme.

Regional preferences are a possible, but difficult alternative. The U.S. could fairly easily offer preferences to Latin America alone, partly because of the historical ties and partly because much of the trade is already entering duty-free or nearly so (raw materials). There would be a problem with Mexico because of the so-called "runaway plant" from the U.S. For Canada or the U.S. to give preferences to East Asia would be very difficult, in view of all the recent pressures to moderate importation of manufactures from this area. Such an action would be seen to be locking the American economy into a "deadly embrace" with the source of most of its import difficulties.

The problem of how to deal with the Eurobloc, and the protectionism of the U.S. and Europe, thus remains a central question, regardless of what happens to the question of general or special tariff preferences. The international politics of any new liberalization effort are a crucial element in assessing its practicality. For example, if Japan were to reverse its practice of passivity or defensiveness in broad international trade policy, and embark on an effort to initiate new thinking around the world, this would certainly have an impact on the U.S. and the European Community. Japan would have to pay something for leadership; she would have to offer trade and investment concessions in return for leading in the achievement of a more equitable international system. Japan could diplomatically help to organize the sentiments and positions of the Asian countries in one or another of the Asian or Pacific discussion forums. This in turn would help to counterbalance the heavy negative influence of the Eurobloc affiliates in the Mediterranean and Africa.

It is my judgment that the developed countries have been able to succeed so easily in restraining Japan and individual East Asian countries because it has been possible to divide them up. As in labor negotiations, concessions gained from one could then be wrung from another. The effectiveness of quantitative import restrictions lies in the way in which they are administered — the category definitions, the licensing procedures, and the degree of administrative discretion. The countries of Eastern Asia have done nothing to try to gain international agreement on rules for imposing quotas on administrative guidelines. Japan could help organize such an effort. While Japan has import problems of her own, even in textiles now, in the long run Japan will most of all want liberal conditions of access for her exports and continuing import pressure to help the process of restructuring industry and moving labor to higher productivity industries.

Alternative forms of regional cooperation are much discussed, and analyzed. One may talk about alternatives ranging from regional cooperation or liberalization among a few of the developing countries, on the one end of the spectrum, to broad schemes of liberalization, such as Professor Kojima's PAFTA proposal, at the other end of the spectrum.

The questions of trade liberalization, and payments arrangements to support regional economic development, or at least development of groupings such as ASEAN, have been thoroughly discussed in various papers. I have nothing to add to the technical discussion, except perhaps to stress that the complementarity question is even more serious now, in the face of the technological changes in agriculture and the consequent self-sufficiency of many countries.

The basic question, as emphasized in the Asian Development Bank study of the Asian-Pacific in the 1970s, is the pattern of industrialization which takes place. This in turn raises the question of how to introduce some modest form of industrial planning which might lead to greater specialization and complementarity. In the light of the various economic and political forces at work, discussed earlier, especially the unemployment pressure which can be expected to rise in the developing countries of the area, this matter should take precedence over simplified trade liberalization and payments pooling schemes.

From the point of view of the developed countries of the area, some further cooperation on specific problems could be undertaken. For example, as regards Australian-Japanese cooperation, Sir John Crawford recently remarked:

> "There is sense, however, in widening the scope of our trade treaty with Japan to provide for full consultation about Japanese investment in Australia (at present relatively small), about shipping, about non-tariff trade measure, and about economic aid to Asia, including joint investment proposals in less developed areas. Initiatives already taken in these matters by Australian and Japanese business interests are to be welcomed and, indeed, are in marked and pleasant contrast to the atmosphere which prevailed in 1957 when the first Trade Treaty was signed. These will be more effective in their outcome if the two governments talk about the relevant policies."[4]

Cooperation between Canada, the U.S., Australia, New Zealand and Japan in aid, trade and investment could be encouraged, to provide an incentive to give shape or design to the economic evolution of their relations with the developing countries of the region, and to consider how best the group as a whole might deal with the implications of the Eurobloc and its affiliations. Discussions along these lines, even if they only led to a few specific ideas, would be better than the present policy vacuum.. Moreover, it would serve as a vehicle for developing the outlines of the economic elements of the "Guam Doctrine," which is best done by the initiation of ideas from other countries in the Pacific. The concept implied in the Guam Doctrine is, after all, American support of Asian efforts and initiatives, as opposed to American initiatives.

Despite the existence of ECAFE, something could be created along the lines of the OECD, for the Pacific Basin, with the objective of providing a better basis for trade and investment liberalization, and coordination of development assistance efforts, in the area. Such a body could also serve as a coordination group for preparing positions *vis-à-vis* the Eurobloc, and perhaps even with regard to the North American market (even though the U.S. and Canada would be members).

There is one task, which would be an important form of trade liberalization, which the developing countries could undertake in concert. This would be to review with each other their respective protection, and

[4] "Economic Prospects for Australia and Its Neighbors," *UMBC Economic Review*, United Malayan Banking Corp., Vol. VI, No. 2, 1970.

export subsidy, policies, to compare notes on experience and to formulate ways in which the mechanisms used might be simplified and made more effective in development policy. The debate over "inward-looking" and "outward-looking" policies ought really now to be carried on between planners and administrators in the various governments concerned. On the question of non-tariff barriers and other sophisticated or complex trade-distorting measures, it would be useful to undertake a review of each other's measures to determine ways in which the measures and their administration might be simplified and put under a general framework of principles. The sheer complexity of dealing with each other is often a deterrent to trade, especially to smaller exporters, and it confuses the assessment of appropriate location of investment.

The broader and more bold conception of a PAFTA as a means of trade liberalization is a different type of proposition altogether. First of all, the internal politics of the key countries in such a group would not allow free trade among the group at this time. Japan, for example, is simply not ready to eliminate all its agricultural protection, nor to align its farm price policies with those of other countries in the next few years. Nor is Japan politically prepared to commit herself to completely free conditions of trade and investment. Australia and Canada are in essentially the same position. The U.S. position would be even more difficult, because of the present troubles with manufactures from Eastern Asia. The only free trade area notion that has been given serious, though limited, thought in Washington is an industrial free trade area with the Western European economic complex.

The PAFTA idea poses basic problems. The EC and EFTA were able to accomplish mutual trade liberalization and allow relatively free investment because, among other things, the countries concerned were near each other in stage of development and their wage structures were similar. There already was a high degree of interdependence in trade when the Community began to function in 1958. The rate of growth of internal trade has been much faster than trade with the rest of the world because of the base of mutual interest. The Eurobloc as a whole with its affiliates, is a controlled variant of the Community structure. Non-members gain access under special, reciprocal conditions. The developing countries with low wage conditions get preferred access only on certain products, and in turn give selected "reverse preferences." The liberalization is tailored to what is in the interest of the Community members, without entailing the costs of adjustment that general free access for these countries would entail. The U.S. internal market, again, is a market built around a comparable wage structure throughout the country. There is still some modest incentive to move from New England to the South, but the differential is small. The accusations once made in New England about "runaway mills" moving to the Carolinas or Georgia are rarely heard now — instead the issue is one of "runaways" to the Far East.

PAFTA for Canada, New Zealand, Australia, Japan, and the U.S. could become politically viable only a little later, when conditions in each economy were more similar, especially in wage structure in relation to productivity. Even then, there would be a question of how to assimilate the Japanese way of business life in the more free system which the U.S. still prefers. Professor Kojima's proposals[5] ought to be given further study

[5] In their most recent form in *Japan and a Pacific Free Trade Area*, Macmillan, London, 1971.

nonetheless. The question of how to create a suitable counterbalance to the emergence of other economic blocs may give the question a meaning well beyond the dimensions of the economic benefits of free trade between four or five countries.

There are of course variants, including on the one side a PAFTA with associated preferential countries as appropriate; and on the other side the NAFTA concept with Japan and Australia in the group, with North America and parts of Europe. The most recent variation is the more sophisticated MUFTA idea. A commitment to move towards free trade is made by a group of countries, on a fixed time schedule. Any country may join which wishes to do so. The schedule can be elongated, and the process of negotiating the treaty of commitment would be an important phase of the work. A number of issues, particularly in the non-tariff area, could then be negotiated piecemeal after the commitment language was agreed to — something like the EFTA experience.

While such a process is likely to match up some unlikely partners, not necessarily regionally tied to one another, it would provide some leverage against the Eurobloc, and it would limit the neomercantilistic tendencies of its own larger members, at least in relation to other members. MUFTA is a form of "conditional MFN." It would allow extension of benefits to be limited to those countries willing to commit themselves to behave toward member countries in certain, predictable ways. Other countries which discriminate against members could face meaningful discrimination against them.

A MUFTA process would perhaps be very useful to countries like Australia and New Zealand. It is less clear what the advantages to Japan and North America would be in the short-run. It would be valuable, for example, if it forced the Eurobloc to participate in a wider liberalization, but the incentive for Europe to do so would not necessarily be great. Two-thirds of Western European trade is intra-European trade, and that is the problem all the other countries are up against.

Another approach to liberalization would be through sector negotiations and commodity arrangements. Some analysts have mentioned the Canadian-American automotive agreement as a prototype. It is a bad example. For one thing, it has not worked in a balanced way, because a relatively weaker country like Canada cannot really open its industry to a relatively powerful one like the U.S. It might have worked if the balance of gain and cost on each side had been worked out very specifically, product by product, but that would have been a very time-consuming negotiation. Moreover, a sectoral agreement in, say, the Pacific, would not easily solve problems with competitors elsewhere, while it would intensify the need for structural change internally. (What would happen to Detroit if Japan were in the group?) A sector approach is more likely to work within an area for a rapidly growing, complex industry which ought to be shaped regionally; or for a worldwide problem. A sector discussion with all major trading countries could result in useful balancing of the conditions of trade and investment, by allowing harmonization of non-tariff as well as tariff problems, and long-range policies. It should not be ruled out, but rather explored with great caution.

Commodity arrangements are possible, and can work, under certain conditions. Regional commodity arrangements are not likely to go anywhere, unless they can really be used to affect world trading conditions.

This is quite impossible in rice or in oilseeds, for example. International arrangements must, again, be approached cautiously. Commodity agreements can only be effective if they are seen both as a forum for discussion of methods of harmonizing national policies and as a method of regulation of the conditions of trade, especially prices and export subsidies. The concept of a commodity arrangement being a price agreement, as proposed in much of the international discussion, is not meaningful. European officials often, for example, speak of the need for "order" in world markets through agreements on the regulation of pricing practices. Price benchmarks tend to be ambiguous, allowing room for shading freight rates, qualities, and terms. Soon after prices are set, production conditions and market demand inevitably alter, so that the price differentials previously established turn out to be unrelated to market conditions. Thus no matter what prices are set, agreements on production controls and/or market sharing soon become necessary to hold prices steady. Alternatively, and in my view preferably, commodity arrangements should have the price element flexible, using prices as a trigger for consultative procedures on other aspects of production and trade policy. The product concerned is also a crucial matter. Tropical oilseeds compete with temperate products like soybeans, which in turn, because of their protein content, compete at the margin with feedstuffs and are demanded as meat and dairy production stimulants. Separating out fats and oils in this context is extremely difficult to do.

On the whole, real progress in agricultural trade will have to come on a global basis, but it may be possible to break out basic sectors like all of grains (feedgrains, wheat, rice).

The basic problems in trade, and this is especially true for the exports of Japan and Eastern Asia, are the basic conflicts in national policy, which often manifest themselves in the form of non-tariff barriers. The GATT framework of rules, procedures, rights and obligations is the most suitable base from which to work on these problems. It is, of course, true that EFTA made great strides on NTB's within a limited group of countries.[6] However, EFTA left out agriculture altogether; and the progress made on other matters was limited to the obvious areas, in which industrial sales would not grow under free trade conditions unless certain other conditions were altered (e.g., certification of technical standards).

Tariffs remain an important element of the picture — especially in the hard core areas where they remain very high in spite of several multilateral negotiations over the years, and where the effective protection on processing is high relatively to protection on raw materials. Non-tariff impediments and distortions are the most difficult to deal with, and are now probably the most important questions in relation to future trade prospects. The question of how and when quantitative restrictions should be applied is a critical issue, particularly in the light of recent American pressures and actions for quotas on beef, steel, ceramic tiles, shoes, textiles, and assorted other products (like canned mushrooms from Taiwan). The restrictions in Europe against Eastern Asia, formal and informal, are important both because of the limitation on access to Europe and because of the effect on American political reaction to imports, in full light of European policies and practices.

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[6] See for example Gerard and Victoria Curzon, *Hidden Barriers to Trade*, Thames Essays, Trade Policy Research Centre, London, 1970, Chapter 3.

In my paper for the President's Commission on International Trade and Investment Policy[7] I argued for a strategy of setting aside the traditional concept of reciprocity, in the sense of horse-trading, and aiming instead at new rules, guidelines, and codes of conduct, coupled with consultative procedures for complaints which can be measured in terms of deviations from these rules, guidelines, and codes. Reciprocity would then take the form of equal commitments by nations, rather than equivalent concessions measured in traditional terms.

This approach sets aside such notions as a "standstill" agreement (sometimes proposed by developing nations), and aims at persistent efforts at problem solving, perhaps piecemeal, through harmonization of national economic policies affecting each sector. Trade liberalization would, following this approach, require elimination or harmonization of many other impediments and distorting policies, so that the conditions for trade and investment would be more neutral, apart from tariffs.

Taking this approach as a basic policy approach, questions like textile restrictions should simply not be discussed bilaterally, where exporting countries can be picked off one by one, unless there is also a multilateral discussion aimed at common principles of imposition and administration of restrictions, and at providing information to all countries on the policies and practices of each. The hard lesson of the last few years' experience in the use of quantitative restrictions, especially "voluntary" restrictions, is that multilateral procedures are sorely needed, to protect exporting countries, and to constrain governments of importing countries from taking precipitous actions on behalf of special domestic interests. Greater emphasis on domestic adjustment measures in the case of labor-intensive industry, in depressed areas, or in agriculture will require greater external pressure. Otherwise, governments will naturally prefer to pass on the costs of adjustment to business interests in other countries, rather than pay out budget money. For this very reason, it is necessary to force these restrictions into a multilateral framework, which might require, for example, that a government imposing a restriction also implement a domestic program to bring about structural adjustment of the industry concerned.

New restrictions do not only harm the interests of the exporters of manufacturers. Australian wool exports do get damaged by the reduction of the prosperity of the Japanese textile industry, which in turn is adversely affected by American restrictions.

If the present general breakdown in U.S. relations with Japan were to continue on top of trade restrictions and other trade and investment problems, Japan could very well decide to reduce her dependence on the U.S. and build up closer ties in Asia, leading to yet another bloc situation. In the end, with India and Pakistan likely to be left out, China restless, and the developing nations nervous about the concentration of Japanese power, I cannot help but feel that this would lead to real political problems.

My conclusion is that another multilateral effort is needed, which is more broadly conceived than past trade negotiations. It is likely to cover many national policy questions if NTB's are truly to be tackled; and it is likely to involve some review and reform of the international institutions and

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[7] "Modes of Negotiating in the 1970s," in *United States International Economic Policy in an Interdependent World*, papers submitted to the Commission on International Trade and Investment Policy, U.S. Government Printing Office, July 1971.

rules. Some of the change would come about through agreement among the major industrialized nations, other changes might take the form of more general agreements.

The shock of the August, 1971, measures may have provided an opportunity to go for a broad effort. In fact, a well conceived long-range strategy would be to have the Group of Ten on the monetary side negotiate some fundamental changes in the monetary system, while the new High Level Group of the OECD does a similar fundamental review for trade and investment. Then, in a year or two, other nations could be brought in to undertake major negotiations, involving reform of the trade policies of all countries (developed and developing alike) and the formulation of rules and procedures which would channel national decisions of the type which affect other countries.

In the end, as remarked earlier, I believe we will want to keep at least those elements of equity and those defenses against predatory behavior which the GATT rules already contain. Throwing these away in the present context would gain nothing, and with the present political balance in the world the negotiation of new rules from a clean slate would be almost impossible to achieve.

In spite of my conclusion that a multilateral effort is needed, and that other nations must try to pull the Eurobloc and the U.S. along a path they have recently been reluctant to tread, such an effort could fail. There are consequently two reasons why some form of regional cooperation and policy coordination are needed. First, the countries of the region must cooperate in order to provide leverage to alter present trade policy circumstances and avoid sliding into a mode of relationship of competitive power blocs. Second, they should cooperate so that if the broad, multilateral approach breaks down, they are not each then hostages of fortune, highly vulnerable to *ad hoc* policies of the three great Western powers, the U.S., Japan, and the Eurobloc.

Pacific cooperation in my view ought to take several forms — some of them are noted in passing in this paper. The matters covered include aid, trade, and investment. Aid and investment policies are important in the development of the area, as well as trade, and the rapid development of the area is essential to help build up the strength it needs to support itself in this present sea of uncertainty and neomercantilism.

COMMENTS BY PROFESSOR G. CURZON

Professor Curzon said that he basically agreed with Dr. Malmgren and he wished there were more such negotiating papers. He noted that he and Dr. Malmgren had often arrived at similar conclusions because if policy-makers are assumed to be bloody-minded, anti-free trade and neo-mercantilist, then the answers to trade and other questions, must be generated by examining possible paths of action and not model building.

Professor Curzon emphasized that Canada, Australia and Japan are the arch-protectionist countries and that there would unlikely be a change in the trade climate until these three change their attitudes. At the Kennedy-Round Canada, Australia and Japan got a free ride at it. It will be the last free ride they are likely to get and unless they change their attitudes they will not be asked again to participate in a world-wide exercise. Also, people should not fall into the trap of trying to propose arrangements between these three countries, for whatever happens with regard to such partial arrangements will be a by-product of the commercial policies of the U.S. and Europe.

Dr. Malmgren, on page one, stressed the importance of U.S. and European agreement as disagreement on policy for the rest of the world and especially the relevance of the Common Agricultural Policy (CAP) to the Pacific area. Professor Curzon thought that the CAP is dying if not yet dead, and that it hardly existed with respect to intra-community agricultural production. Its main purpose was to discriminate against third countries, especially against the United Kingdom for negotiating purposes. Since the French-German revaluation and devaluation has been shelved, there are four different agricultural customs territories in the union. The German Agriculture Minister further said that even if Germany had a chance to return to fixed exchange rates, it would not return to the Common Agricultural arrangements.

Professor Curzon suggested the comments on increased protectionism in the U.S. can be looked at in two ways. The U.S. can be viewed as becoming more protectionist, or it can be said that, as part of the general move toward free trade over the past 10 to 15 years, as might be expected problems have arisen that perhaps have not been handled in the most imaginative way, but which should be little cause for pessimism.

It was mentioned earlier that the multinational corporations are potential movers of capital into the most profitable areas. However, Professor Curzon thought they are not as rational as is very often assumed and they are especially not combative enough. He wondered what they maximize, for they are very lazy and tardy about maximizing profits. He said they behave like a chameleon — rather than influencing policy, they look at the policy and adapt accordingly. He also suggested, in answer to a previous question, that they do not charge lower prices after moving to an area of lower costs because they do not know how long conditions will last, for they might have to move back to the previous pattern.

Professor Curzon agreed with the pessimism over general preferences and thought they might even have the negative effect of making the less developed countries bitter.

He was less pessimistic in the sphere of agriculture and commodity agreements in a regional or longer arrangement because of the success of the EFTA agricultural policy which was thought to be non-existent. A forthcoming paper by V. Curzon shows that in the EFTA context, the countries somehow established a "self-sufficiency index" such that when this index is less than one, there exists scope for negotiations with other suppliers of agricultural products. It is an amazing piece of institutional gadgetry which has nothing to do with economic efficiency, but is somehow the price to pay if the countries want to get freer trade in other than agricultural goods. This would have important implications for countries which require some sort of agreements on agricultural products before negotiating about other commodities.

Professor Curzon was rather doubtful about the new principle of more global arrangements arising from the evolution of reciprocity in international agreements. He said the kind of agreement that comes out of international institutions, conferences or negotiations is a framework agreement which specifies minimum concessions, duties and obligations, called the "macro-action". Given the framework, bargaining over implementation, or "nucro-action" begins and this involves horse-trading and reciprocity. He doubted that this process could be avoided.

Professor Curzon made a number of broad points concerning the overall evolution of commercial arrangements and institutions. From an egocentric point of view, the arrangement between the community six could grow gradually to become an arrangement between some ten countries, for example. It is possible non-African countries will ask to be associated with the African countries in their arrangement with the European Economic Community. For the negotiations starting next month (November, 1971) the European Economic Community has accepted the notion of a free trade area arrangement so that many more countries will now be able to talk to the Community than before. Another point was that if the Nixon measures are dismantled, trade arrangements will not return to what they were previously, but rather will move in the direction of freer trade. However, there will only be a move toward freer trade in industrial products among the industrialized countries whoever they may include. But Japan will be in trouble, for Japan wants as close an association with others in trade matters as possible, but other countries do not want Japan. Professor Curzon was pessimistic that Japan itself would take initiatives since Japan is not yet in this mood. Therefore, the global arrangements will be those between the U.S. and Europe and he hoped they would include the U.S. and not be Eurocentric.

Professor Curzon mentioned one proposal that Dr. Malmgren had not made. He said that if the countries of the Pacific region were to have industrial planning, they must engage in some simple forms of trade liberalization. This could be brought about by a preferential trade arrangement rather than by a free trade arrangement. Since they are all very high tariff countries, they could accept a 50 percent preference between themselves and still leave a certain amount of protection in regard to their partners. Such an arrangement would lead to the evolution of a rather natural pattern of specialization and could also be reconciled with GATT. It might be a first step for countries which are basically protectionist-minded, but need to do something jointly. This might also get them some kind of bargaining position in a world which is going to be very tough.

DISCUSSION OF DR. H. MALMGREN'S PAPER

A U.S. participant took note of the emphasis in the paper, comments and previous discussion that the European Economic Community is quite restrictive toward the U.S. and others and will likely be joined by a 50-country bloc approximately, that competition from the less developed countries will become increasingly threatening to the developed countries and that this threat can be most constructively met by appropriate adjustment schemes. He said that if the developed countries do manage to devise positive and fairly comprehensive adjustment schemes, then a Pacific Area Free Trade Agreement (PAFTA) begins to look much more attractive as a second best solution to trade distortions. At the first Pacific Trade and Development Conference, PAFTA was criticized on the grounds that a global approach was better. But, if the European Economic Community is not willing to take a global approach, then there is no reason to reject American-Japanese cooperation in building a PAFTA that would include the other 50 non-communist nations. He said the alternative implication is that the U.S. cannot get along with Japan because Japan is too competitive. But that means that the U.S. cannot get along with any highly developed country and thus that the U.S. might as well close its doors to the rest of the world, to the great harm of both the U.S. and the rest of the world.

Another U.S. participant emphasized that concerned people must think very hard about what can be done in the U.S. and Canada to bring about the miraculous possibility of freer or free trade in the Pacific at least. Professor Curzon said that current problems are a counterpart of the movement toward free trade. This participant said the means to solve these problems are known, but how to implement these means is not known. He emphasized that there is no hope now in the U.S. for reinforcing the freer commercial policies achieved, for there is unquestionably a retreat from these. The interest groups that had previously supported the moves toward free trade — the government executive and the labour unions to some extent — have now joined the protectionist camp. The executive has political commitments to the textile workers in the South and the labour unions have become extremely intransigent against liberal policy. He challenged the people at the Conference to make practical suggestions of how to reverse this trend before it is too late.

A Canadian participant emphasized that the current situation is a disastrous one into which the United States dragged everyone. He was very surprised at Professor Curzon's remarks, for he said there is no question that the failure of U.S. policy in the last few years to take essential actions, particularly on the balance of payments question, but also on other questions related to Pacific relations more directly, has caused very difficult problems in Pacific relationships. The balance of payments problem is not due purely to the U.S. inaction but also to European inaction. However, the U.S. continually talked about the desirability of the status quo, fixed exchange rates, and so on and then, all of a sudden it accepted the notion that the exchange rates were not correct, and needed realignment and consequently took the extreme action that put everyone in the mess that exists today. The U.S. was the only one that could have created the change since the European and central bank attitudes must be accepted as given.

Also, this participant said, it is necessary to be clear about the lack of relation between the balance of payments problem and trade problems in the Pacific. A case has not been made on non-tariff barriers, although it undoubtedly exists, but until it is made, it is not possible to expect Japan or any other country to be susceptible to tough bargaining. Thus a threat that overhangs all Pacific relations is arising out of what could be a myth, or if not a myth, a doubtful proposition that there has been a relative increase in non-tariff barriers in recent years. Therefore, he called on the U.S. to form its own action committee to study and propose solutions to this formidable array of protection. He said the U.S. must take the responsibility for this, since it at least sees some of the light.

Since Japan, Canada and Australia have more protection than other developed countries, the Canadian participant said they of course should not be proud of it, however, people should recall that they regarded the GATT mechanism, to some extent, as inappropriate to their needs, if only partially free trade were considered. However, contrary to Professor Curzon, it is because these countries need more liberalization than anyone else that there is a real possibility of initiatives from them. Although somewhat sceptical about what will happen in these matters, he agreed with Dr. Malmgren that Japan must take very seriously its role in these matters.

An Australian participant commented that any agreement between Dr. Malmgren and Professor Curzon was very subtle and if it existed, his position was far from theirs. He said that Europe and the U.S. largely prevented Australia, Canada and Japan from getting involved in trade liberalization in the post-war period and that people must think carefully about how this situation evolved before pinning the blame on these three or four, including New Zealand, for being free riders at the Kennedy-Round. They were certainly not free riders in agriculture and if Europe and the U.S. continue to try and exclude agricultural products from trade negotiations, Australia and the others ought to start, and will start, looking quite closely at special arrangements with Japan. The Common Agricultural Policy is not dying and if it is, it will take a very long time.

This Australian participant agreed with Dr. Malmgren's shift in his summary of his paper to stressing the need for regional initiatives and also agreed with Dr. Malmgren's assessment of the situation regarding initiatives from the U.S. He said his optimism was contained in the approaches suggested in Sir Crawford's paper and that initiatives to curb protectionism in the Pacific must come from Japan and, to a lesser extent, Australia. He said there was some basis for his optimism but not a great deal, since he was a little more doubtful about Japan's position than Australia's. He suggested new levers would be very useful to assist in removal of some of the obstacles to trade, instead of the head-on clashes that have characterized the textile negotiations and to some extent the present negotiations. He wondered why there was an almost pathological caution in the U.S. with regard to taking initiatives in the Pacific. He also wondered why the Japanese government seems to be retreating to some extent from regionalism and opting for bilateralism in relations with the U.S. when bilateralism looks utterly disastrous.

Professor Curzon replied to the Australian participant that he did say Australian policy-makers were neo-mercantilist, but that he was not trying to place blame. The purpose of the conference was to try and produce a framework for nationally self-interested policy action that was better than the traditional one. It seems that this is more difficult to do for a group of

countries with high levels of protection than for a group which has basically accepted the idea that perhaps protection is not the best policy, although as the Canadian participant said, perhaps this is exactly why these protectionist countries should be more concerned.

A Japanese participant described Japan's position as being pessimistic about global liberalization since only an enlarged European Economic Community is on the horizon. The Japanese government would take a position on trade policy that was neither progressive nor regressive with respect to other countries. In this kind of trade policy in disguise, the Japanese government might actually pursue regional integration with Australia and the Southeast Asian countries, and Canada would be welcome to join. As well, the Japanese government will pursue a policy restructuring its economy so that it will be in an advantageous position for global free trade around 1980. Japan wishes to go along with the U.S. ultimately, but the U.S. is at present too big and too tough. Pacific integration is a good strategy.

Another American participant suggested that the next year would be a very opportune time for initiatives by other Pacific countries toward a proposed Organization for Pacific Trade, Aid and Development to be put on the table by Canada, Japan, Australia and New Zealand. The U.S. would not be able to afford not to participate in it. This forum would provide an important avenue for Asian less developed countries to coordinate their decisions regarding future voluntary export restraints. If they approached the U.S. multilaterally or regionally on issues like textiles, as Dr. Malmgren said, they would achieve much better results than if they pursued bilateral negotiations. He also noted with respect to Professor Curzon's remarks that since multinational corporations are oligopolists, they can operate very effectively in non-competitive situations, such as a protectionist world. He mentioned that Japan is second only to the U.S. in having the largest number of very large corporations and he hoped their multinational corporations would operate in Asia and Europe to more effectively benefit the less developed countries.

In regard to the U.S. policy of response to initiatives on the part of Asian countries, another American participant said this should be interpreted more as responsiveness to initiatives on the part of developing countries rather than Pacific developed countries. The interpretation emphasizing the role of the developed countries gives more weight to a regional design, for attempts of regional positions on the part of the less developed countries have so far not made too much progress, although this is something that could be fostered. He also endorsed the pessimism regarding general preferences of both of the commentators; however, he suggested that pessimism has already been discounted by the less developed countries and they would not count much on preferences.

This participant also stressed the emerging problems of the inability of less developed Asian economies to absorb the immensely increasing supply of labour that flows on to the market each year. While mentioned in Dr. Malmgren's paper, it was not stressed enough, for in the very near future it will overshadow many of the problems discussed at this Conference. The problem has been neglected to the extent it has because not only is data lacking in many cases, but existing data is also often misleading. The data is very little related to reality because the kinds of concepts, definitions, questionnaires, and so on, are Western ones which do not represent the nature of underemployment or even unemployment. The

real situation tends only to be observed when crises result from the problem. Thus a very important question that must be asked is how trade policy can be used to ease this situation and the political mind will respond more to these questions and answers than anything discussed so far at the Conference.

A participant from an international institution said the situation regarding general preferences, while difficult, was not impossible. Although the effects of the scheme are small, Taiwan has been excluded and Hong Kong will not gain much, other Southeast Asian countries — Singapore, Malaysia, Thailand, Indonesia — are now just trying seriously to get into export markets. If they go after products in which they have a comparative advantage and which has not yet been closed off by the scheme, they may get that certain initial edge. A self-defeating attitude, such as the Prebisch line in the 1960s, on these matters is disastrous.

Also with respect to Dr. Malmgren's comment on pages 277 and 278 mentioning the usefulness of complementarity and planning, this participant emphasized that the Asian Development Bank study mentioned actually inveighed against the emphasis on complementarity and rational industrial planning. The greatest gains are to be made from competitiveness in trade not from complementarity. This participant also, criticized GATT for becoming a kind of sacred cow that people are prepared to drive around rather than slaughter because it was based on the most appalling economics.

The participant from Singapore made two comments, one emphasizing the importance of commodity agreements, such as in tin, to the less developed countries and one pointing out that the Nixon measures had little effect on the Southeast Asian developing economies.

Finally, Dr. Malmgren replied to the various comments on his paper. He suggested that if GATT were discarded, nothing whatever could be built in its place, so that it was absolutely necessary to use GATT as a foundation on which to build better regulations. He said that if the U.S. were prepared to implement an adjustment assistance programme, then PAFTA would become a real possibility. However he doubted, because of the opposing interest groups, especially labour, already mentioned, that adjustment assistance would be realized in the near future. He emphasized that it would be completely impossible for the U.S. to go along with any liberalization in industry without a major change in agriculture, but this means running up against Japan and the Common Agricultural Policy. Japan's long-run interests would require buying off all its farmers and their cutting back production sharply within two or three years, but that will not happen, partly because economists have done a bad job of explaining the costs and benefits of agricultural policy. He also noted that the only country in which NTB's have *increased* in the last few years has been the United States.

He suggested U.S. Policy is not concerned with the Pacific area because the fundamental thrust of U.S. policy has been oriented to European security. European integration was sponsored not on the basis of economic reason but rather clearly in order to build up the defence capability of Western Europe against what the U.S. saw as the Soviet threat. In the Pacific, the U.S. has no conception of a massive threat, whether or not it exists. There is also the desire to disengage from Vietnam that shapes the feelings of policy-makers. Thus it is difficult to get the policy-makers, who are basically not economists, to focus on the evolution of the Pacific as an economic problem and what this problem might lead to in terms of stability.

The unemployment problem in Asia is the most important of all, and will have probably the most important long-term security implications for the U.S. The governments of countries like Japan and Australia must simply drag uninterested U.S. officials into the area. Moreover, the downword protectionist slide in U.S. politics requires a concerted effort by other countries to make this a debacle in foreign policy terms.

Appendix

APPENDIX

List of Participants

AUSTRALIA	P. Drysdale, Australian National University
	R. H. Snape, Monash University
HONG KONG	R. Hsia, University of Hong Kong
JAPAN	K. Hemmi, University of Tokyo
	K. Kojima, Hitotsubashi University
	R. Komiya, University of Tokyo
	S. Okita, Japan Economic Research Centre
SINGAPORE	Lim Chong Yah, University of Singapore
UNITED STATES	D. G. Johnson, University of Chicago
	H. B. Malmgren, Overseas Development Council
	H. T. Patrick, Yale University
	A. Paul, Asia Foundation
	J. D. Richardson, University of Wisconsin
	D. Sherk, Simmons College
CANADA	H. E. English, Carleton University
	G. Hainsworth, University of British Columbia
	K. A. Hay, Carleton University

H. Johnson,
University of Chicago and
London School of Economics

A. Litvak,
Carleton University

C. Maule,
Carleton University

A. E. Safarian,
University of Toronto

INTERNATIONAL ORGANIZATION and Others

G. Curzon,
Geneva

H. Hughes,
I. B. R. D.

H. Vandendreissche,
O. E. C. D.